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An Adirondack View

Well, **Segregation** is the subject of current conversation — including some ments. But homo sapiens gets all the tion, just as though he were the only in the world. Let's look around.

Behold the cows, the horses, the ca the dogs. Color lines? None. Black, and red all in one is common. Segreg is for the birds.

And for accountants. We keep the diff expenses from getting mixed-up with other. We won't allow asset costs to li the expense subdivision. We are the s segregationists. When better segregation tems are built, we will build them—or them.

LEONARD HOUGHTON,
Saranac Lake Branch
the "Adirondack Chap

Professional Calendar

Albany Chapter

December 14, Joint meeting with Alba County Bar Association on federal incon taxes.

Binghamton Chapter

December 11, Monthly meeting and technic session on federal income taxes to be pr sented by the Society's Federal Taxati Committee (Carlton Hotel, Binghamton

Buffalo Chapter

December 4, Monthly meeting and technic session—"Recently Issued Regulations U der the 1954 Code"—to be presented the Society's Federal Taxation Committe

December 10, Technical meeting with joi sponsorship by Canisius College on "T Problem of Overhead Costs" (Canisi College).

Mid-Hudson Chapter

December 19, Dinner and technical me on New York State Income Taxation (Newburgh).

Nassau-Suffolk Chapter

December 8, Tax meeting (Southward Club, Bayshore).

Richmond Chapter

December 11, Public relations meeting wi internal revenue agents (Irondequoit Cou try Club).

Syracuse Chapter

December 13, Meeting with local bank (University Club).

New York City

December 5, General meeting; featur speaker—Dr. Marcus Nadler (Hotel Roo velt).

December 10, Technical session, Committ on Problems of the Individual Practition (Engineering Societies Building).

December 12, Technical session, Committ on Graphic Arts and Allied Industries A counting (N. Y. University Club).

December 13, Technical session, Committ on Entertainment and Sports Accounti (N. Y. University Club).

December 17, Technical session, joint sp sorship, Committees on Real Estate counting and on Federal Taxation (En neering Societies Building).

December 19, Technical session, Committ on Fiduciary Accounting (Engineering cieties Building).

Book Reviews

Appraisal and Management of Securities

By Douglas A. Hayes. THE MACMILLAN COMPANY, New York, N. Y., 1956. Pages: viii + 383; $6.00.

Since Prof. Hayes (now Professor of Finance at the University of Michigan) was formerly associated with Price Waterhouse & Co. and with the Investment Counsel, Inc., he brings to this interesting, brief and competent text, a practical background of accounting, finance and investments. The result is a cautious and modest approach and an intelligent analytic appraisal of investment risks and opportunities.

Eager opportunists will find no heretofore undisclosed formulas whereby investors can "get rich" either in short order or over a number of years. Prof. Hayes states flatly that those who profess to have methods of practically assuring remarkably favorable results on an investment account are either uninformed or charlatans. His emphasis is on probability. He believes that sound selective judgments and decisions will, over a period of some years, increase the probability of satisfactory results to a significant but moderate degree. Thus, this book is not for those who believe, with Somerset Maugham, that "it is better to be lucky than clever."

The volume is divided into four parts: the first on approach and limitations deals with the scope of investment operations, the investment characteristics of securities and ends with a theory of investment operations. The second is devoted to an appraisal of investment characteristics and is divided into the qualitative and quantitative appraisal. The third, on determination of investment standards and values is divided into two chapters on the selection of fixed-income securities and two on the selection of common stocks. The final portion of the book is on the management of security portfolios.

Like most good investment texts this one has a definite philosophy and outlook. Prof. Hayes does not believe in trading operations. Nor does he believe in the popular approach of attempting to profit by buying securities during the early stages of a major bull market and then selling out before a bear market gets under way. This is the old adage of "buy 'em when they are low and sell 'em when they are high." It is, of course, as Prof. Hayes points out, much easier to say than to do. Most individuals, he suggests, would be well advised to ignore market predictions per se in their investment decisions.

His philosophy is the purchase of common stocks in well-established companies as a long-term investment. He observes that the shares of very reputable companies, taken as a whole, have shown a gradual but unmistakable upward long-term trend in market price even though variations around the trend have been relatively great. He points out that investors who have bought and held a diversified group of such stocks for long periods have enjoyed a considerable amount of appreciation in addition to dividend income.

"Basic conceptual differences," he declares, "are involved in investment for long-term appreciation as compared with the 'buy-low sell-high' approach. In the first place, common stock commitments are approached on the presumption that they will be permanently held in the portfolio. Therefore an analysis of market prospects per se has little, if any, part in investment techniques based on this objective. The aim is to obtain common stocks which are selling at reasonable prices relative to their appraised value, and one of the elements of such value is the prospects for the companies gradually increasing in economic stature throughout future years. . . . In the second place, under the buy and hold theory the investor in common stocks does not expect results in the form of appreciation to be spectacular or immediate. The success or lack thereof of an investment in common stocks should be measured over a decade or so."

The chapters on common stocks and on portfolio management are devoted to an analysis of techniques for the successful pursuit of such long-range investment, that is to the selection, at proper prices, of securities in companies which are likely to move forward and provide major appreciation over the long-run. While Prof. Hayes' approach to investments will appeal to the cautious and patient, it will hardly have much interest for the more numerous who look for "hot tips," "play the market" and expect a doubling of price in 181 days. Over a lifetime, the former will probably build substantial estates, while the latter, despite some occasional spectacular gains, are likely to "go broke."

JEROME B. COHEN

Baruch School of Business and
Public Administration
The City College of New York


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The New Tax Law in Action

Published for the Texas Society of Certified Public Accountants by THE JOURNAL OF TAXATION, INC., New York, N. Y., 1956. Pages: 241; $4.95.

Most accountants who find their heads still spinning from all the substantive changes incorporated in the Revenue Code of 1954 will welcome *The New Tax Law in Action* which is a compilation of papers presented at the Second Annual Institute of Taxation conducted by the Texas Society of Certified Public Accountants at the University of Houston in November, 1955. Far from being a comprehensive review of the code, the publication merely presents the experience of sixteen practitioners with the workings of some of the more commonly encountered tax problems.

A Houston CPA starts off the proceedings with a highly competent review of the penalty provisions aimed at preventing use of corporations to evade or avoid taxes, and then goes on to consider how corporations might still be used to save taxes notwithstanding these penalties. In the area of corporate distributions and liquidations, where the volume of literature has already reached staggering proportions, the writer, hampered by the absence of final regulations at the time of his writing, attempts to give a brief resume of each of the relevent tax sections. Unfortunately, the resumes are a bit too skimpy even for a short generalized study.

The complex code sections relating to termination of partnership interests, partnership contributions, retirement plans, life insurance and annuities, depletion, oil payments, joint ventures, livestock, operating losses, and transactions between related taxpayers, are each highlighted in separate stimulating papers. A brief yet highly lucid article on the subject of depreciation is featured as a comparatively "simple" topic—but only when compared with the other federal income tax problems with which the practitioner finds himself submerged.

In the paper devoted to the preparation of an estate tax return and related problems, the author successfully uses a case study technique to outline the problems growing out of the 1954 changes. That is followed by a separate paper on income taxation of trusts and estates which offers a rather superficial review of the subject. It is unfortunate that the two authors missed their opportunity to coordinate their separate discussions by applying the income and estate tax sections to one case study report.

A paper on the problems relating to community property may not be of particular interest to a New York accountant since it focuses its discussion on the Texas community property system, but unlike any of the other articles, the paper does conclude with a rich detail of footnotes.

Although definitely not a major work, the compilation should offer the practitioner a highly useful survey of a vast new area and as such is highly recommended for a tax library.

SAMUEL A. DYCKMAN

New York, N. Y.

Letters to the Editor

Reporting Standards and the Disclaimer

Independent certified public accountants are becoming increasingly aware of the reporting requirements resulting from the adoption in 1949, of Statement on Auditing Procedure No. 23. However, certain aspects of this statement (especially relating to long-form reports and to "special" types of reports) would seem to be in need of clarification and refinement.

Does anyone wish to comment in the columns of your magazine on the following set of facts:

> An auditor is not present at the inventory count nor can he satisfy himself by other procedures, he therefore disclaims an opinion and states the foregoing circumstance as his reason for the disclaimer. However his examination discloses departures from generally accepted accounting principles and/or deviations from their consistent application, either related to inventories or to other items.

Since the auditor is disclaiming an opinion, need his report also point out and explain the departures from accepted principles or con sistency?

Some practitioners may believe that if they have disclaimed an opinion for an auditing reason, there is no need to add to the language of their disclaimer.

This may stem partially from the emphasis on the audit examination in the discussion on reporting standards set forth on page 14 of the 1954 edition of *Generally Accepted Auditing Standards,* published by the American Institute of Accountants.

> "The report shall either contain an expression of opinion regarding the financial statements, taken as a whole, or an assertion to the effect that an opinion cannot be expressed. When an over-all opinion cannot be expressed, the reasons therefor should be stated. In all cases where an auditor's name is associated with financial statements the report should contain a clear-cut indication of the character of the auditor's examination, if any, and the degree of responsibility he is taking."

However, the other three reporting standards also relate to this problem. They are quoted below:

> "The report shall state whether the financial statements are presented in accordance with generally accepted principles of accounting.
>
> The report shall state whether such principles have been consistently observed in the current period in relation to the preceding period.
>
> Informative disclosures in the financial statements are to be regarded as reasonably adequate unless otherwise stated in the report."

This leads to a related and often troublesome problem. What is the accountant's responsibility for reporting, in the disclaimer letter, violations of accounting principles relating to asset valuation, particularly as to inventories? Should the auditor confine his disclaimer purely to the auditing limitations or should he clearly set forth the additional factors relating to accounting principles which alone may be sufficiently material to require a disclaimer?

If sufficient readers respond, a basis may be established for a further clarification of standards of reporting for disclaimers.

STEPHEN CHAN, CPA
New York, N. Y.

Pro-ration of $1,000 Exemption—Partial Years of Estates or Trusts

At the conclusion of my article (*New York State Income Tax Problems Relating to Decedents, Estates and Trusts*) in the October 1956 issue of the *NYCPA,* I stated that my objective in writing the paper was "all in the hope of helping us to avoid some of the booby-traps which are bestrewn over our course." It now appears that, with the best of intentions, I have laid just such a booby-trap when near the top of page 605 I said:

> "5. An exemption of $1,000 is allowed to the estate. This exemption is prorated for taxable years of less than twelve months."

On this score, it is urged that the readers "follow the forms" (a procedure which, ironically, I deprecated in the opening paragraph of my article). Thus, the instructions for form IT 205 state as D3:

> "An estate or trust is entitled to an exemption of $1,000 in ascertaining its tax liability, whether the period covered by the return is for a full year or less."

I regret any inconvenience caused to any of our readers by the omission of the errant "not" in the subject paragraph of the article, which should have read:

> "5. An exemption of $1,000 is allowed to the estate. This exemption is *not* prorated for taxable years of less than twelve months."

I would appreciate your communicating these facts to your readers.

ABRAHAM J. BRILOFF, CPA
New York, N. Y.

Education No Substitute for Experience

Since New York State has long since achieved the interim requirements suggested by the Standards Commission, this State and its C.P.A. Society might show the rest of the nation the way toward the ultimate goals set up, if it is felt these goals are worthwhile.

My understanding of the Commission's major recommendation is that additional education be substituted for the experience requirement. It is argued that accounting is a body of knowledge that can be taught in a classroom without reference to experience. The only thought advanced in favor of this unproven argument that I have heard is what might be called the trend argument. If the present requirements of 4 years of college and 3 years of experience is better than the no college and 10 years experience requirement of a generation ago, then 6 years of college and no experience should be still better. I have never before heard any practising C.P.A. say anything that implied that the experience requirement should be abolished. On the contrary it seems to me that most accountants believe in a golden mean of balance between education and experience.

The general complaint concerning young men in accounting is not that they are short of book learning but that they are deficient in practical knowledge. Does not this policy tend to weaken our newcomer's weaker side in order to provide time to strengthen his stronger side?

The general complaint concerning more experienced practitioners is that once they acquire certificates, there is a tendency to stagnate academically. A system in which study ceases entirely about the time experience begins, certainly does not encourge continuing study (a real problem of our profession).

A three-month internship would be excellent training for a junior accountant, if the tremendous practical problems could be worked out. But it would hardly be enough for a C.P.A. unless we reduce the meaning of a C.P.A. to something resembling a highly educated junior.

I can see much merit in aptitude examinations to discourge those who are obivously unsuited to public accounting and in requiring a more rounded, liberal education, but, in my opinion, to substitute a masters degree for half of the present C.P.A. requirements would be a poor substitution indeed.

LOCKE GRAYSON, CPA
New York, N. Y.

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The President's Page

Behind the Scenes

The actual operation of the Society's offices at 677 Fifth Avenue is a mystery to most of the members. The outward manifestations of activity are, of course, visible. We receive *The New York Certified Public Accountant* and the *CPA News* bulletin every month, dues bills come as do membership directories, lists of officers, directors and committees, annual reports and notices of meetings. Committee chairmen are aware of and appreciate the support they receive in arrangements of space, notices of meetings and processing of minutes. But generally the members may feel that it is an impersonal organization, a modern mechanized operation, a well-constructed robot that functions for the Society, which in September alone sent members 162,000 pieces of mail.

Of course this is not so. Those who serve you in the Society office are people—people skilled in their work. The Executive Secretary, Harry Howe, came to us with a wide background in management, trade association and public relations work. Gilbert Desvernine, who is in direct charge of public relations, spent eight years with Ivy Lee—T. J. Ross, one of the most prominent public relations organizations in the country. Dorothea Legenhausen, who, among other duties, coordinates the work of our seventy committees and who is present at our board and executive committee meetings, is a graduate lawyer. Ben Newman, the new editor of *The New York Certified Public Accountant,* earned his B.A. and M.S. degrees with majors in English and his M.B.A. with a major in Accounting. He is also a certified public accountant. These are samples of the backgrounds of the staff.

The members of the staff, most of whom have been with us for only a year or so, have been formed by Harry Howe into a remarkably good team. Each has his or her functions and responsibilities and each must do these competently. In the direct touch with members, Bernita Wedeking handles membership relations with a fine directness and great tact; Glenda Small greets the personal visitors and the telephone callers with a ready smile and a pleasant voice. Peggy McShane is meticulous and thorough in the billing of dues and their collection as part of her keeping of the books and accounts of the Society. Ben Newman is stimulating the members in his new and challenging task as Editor of the CPA. The helpful and experienced background of Sarah Genova was vitally important during our recent editorial change of the *NYCPA*.

In the background are the excellent secretaries: Ruth Steele and Paulline Romandetta and the others who serve anonymously, but efficiently; Joan Spielmann, Marilyn Goldblatt, Debra Klem, Theresa Ceci, Nada Mavrovic, Pearl Weinstein, Dan Crowley and Bill Uzoaga. The direction of the latter group is under an able professional office manager, Leila Egenites, who is also constantly finding, with her assistants, new ways to do things more efficiently and more competently.

There is a deep spirit of friendly cooperation—of "backstopping" one another—that flows from Harry Howe through all of them.

The emphasis on competence and team work may still leave the impression of a machine, but the staff members are distinctive human beings. For example, the operator of the multilith equipment, Bill (Okefie) Uzoaga, who is from Nigeria, has only eighteen months of work to complete for his Ph.D., Dan Crowley, the addressograph operator, writes music as a hobby, Bernita Wedeking is a singer, Gilbert Desvernine has a keen interest in things French, having lived in France and sailed his own boat on the Seine, Leila Egenites can talk knowingly of marjoram and sweet basil, tarragon and rosemary.

It is indeed a fine team!

ARTHUR B. FOYE,
President

Accounting for Investments In Jointly-Owned Associated Companies

By Eugene L. Zieha

An increasing number of corporations are cooperating with one another through the formation of jointly-owned associated companies. This article discusses the reporting and accounting practices relative to this type of corporate relationship and considers certain of the applicable fundamental accounting and reporting problems.

Background and Definition

The formation or acquisition by major corporations of an increasing number of *associated companies* represents a significant addition to the pattern of American business organization. Many prominent corporations are engaging in this modern counterpart of the joint venture by establishing associated corporations whose stock is owned exclusively by two or more other corporations. There are enough examples of companies owned in this manner to suggest that the well-informed accountant should be aware of their existence and of some of the basic problems inherent in accounting for them.

Accounting usage is presently developing a technical meaning for the term "associated company." In his *Dictionary for Accountants,* Eric Kohler gives a first definition of an *associated company* as "a corporation exactly 50% of whose voting capital stock is owned by another." The expression is not widely used and some accountants use it to refer to stock ownership of a significant amount but not above 50%. The discussion in this article is limited to cases in which the associated companies are owned or controlled *completely and equally by two other companies.*

A small number of such jointly-owned associated companies have existed for many years, but in the past few years their number has grown rapidly. A private survey of the published annual reports of more than seventy five companies that participate in this type of

Eugene L. Zieha *is an Associate Professor of Accounting at the School of Business, Air Force Institute of Technology, Wright-Patterson Air Force Base, Ohio. He holds degrees of M.S. in C. from St. Louis University and Ph.D. from the University of Illinois. Dr. Zieha is a member of the American Accounting Association, the Federal Government Accountants Association and the National Association of Cost Accountants.*

joint ownership provided background material for this article. Appended to the article are tabulations which classify seventy seven of these owning companies by net worth and industry. After a brief discussion as to the type of companies under consideration and the reasons for their existence, attention is focused on the accounting problems inherent in this joint ownership.

How should this ownership of 50% of the associated company be treated on the balance sheet of the owning companies? How should income from the associated company be recognized and reported? Here is a special situation which is not covered in the normal methods of accounting for the ownership of stock of another company. While these problems are not necessarily serious as regards the entire area of accounting theory, they are of major concern to the accountant faced with them.

Reasons for Formation of Associated Companies

Why do the managers of two corporations decide to form a third corporation that is to be jointly owned? At times the text of corporate annual reports, publicity releases and other publications explain clearly the reasons for the new organization. In other cases, the apparent reasons can be obtained by considering the type of activities in which the companies involved are engaged.

A common reason for the use of the form of corporate relationship under consideration is the complementary nature of the resources of the participating companies. These are frequently utilized in the introduction of a completely new product. For example, a producer of basic materials may cooperate with a firm skilled in the manufacture and distribution of a product utilizing a newly-discovered synthetic material. Likewise, a company which has a sizeable quantity of a by-product of a basic nature may join with a chemical company in the formation of a corporation that will produce chemical products from the by-product. In one outstanding case, scientists of a motor company and an oil company joined hands in research and led the way to the formation of a company to produce a product to improve gasoline.

Frequently, competing companies join together to form a company that will supply them with a basic raw material or service. Numerous examples exist in the development of sources of iron ore by the large steel companies. Service facilities of a semi-public nature, whose duplication would be unwarranted or physically impossible, are especially appropriate for this type of organization. Dock facilities, pipe lines and parking lots are in this category. The basic idea is to make available a service from which both companies would benefit but which each company would be reluctant to finance and operate on an individual basis.

In some cases an operation may be too large for an individual company, and the authorities able to grant the necessary rights to operate may not desire to give a contract to one company. This is the situation prevalent in the development of the oil resources of some foreign countries. The laws of another country often force this type of organization upon the foreign company that desires to do business there, in order to encourage local participation in certain industries. The research undertaken by the writer in the area of associated companies has excluded consideration of foreign operations unless the foreign aspect was accidental in nature.

General Accounting Theory

Commonly followed accounting practice provides two methods of presenting

the ownership of stock in another corporation. If a number of qualifying conditions are met, the accounts of the company whose stock is owned are consolidated with those of the parent company. If the required conditions are not met, the stock ownership is carried as an investment under an appropriate balance sheet heading.

Two major tests are used in determining if the accounts should be consolidated. The first, requiring ownership of more than 50% of the subsidiary company's stock, is based upon the certainty of control. Accounting practice and various regulations pertaining to statement presentation normally require that ownership be considerably in excess of 50% before consolidation takes place. The second test is based upon the compatibility of the accounts to be consolidated. A scheme of accounts reflecting activities completely foreign to those of the parent company would not be consolidated. Once the minimum conditions are met, the accountant must exercise judgment in determining the appropriateness of account consolidation. The important question is whether the financial position and operations are more clearly expressed by the consolidated or the non-consolidated statements.

According to the above tests, the accounts of jointly-owned associated companies should not be consolidated in the statements of either of the owners. Since each company has a 50% interest, neither one meets the minimum requirement of assured control. But a further thought may be that, inasmuch as this is not the ordinary type of parent-subsidiary relationship, the tests given do not apply. Such reasoning would require the establishment of new accounting practices to cover this situation.

An alternative method of accounting for the stock ownership is to treat it as an investment. Ordinarily, investments are carried at cost, although the balances could be reduced below cost if a material decline in the ascertainable value of the investment occurred. At times the market value of the investment, or the proportionate equity per the books of the owned company is provided as additional information.

The stock ownership under consideration is a peculiar type of investment insofar as accounting is concerned. While the cost should be readily available, the owning companies frequently have direct or indirect commitments that may affect such cost. The market value will not be easily ascertainable because no securities of the company are being traded. Unless disclosed by the two owning companies, financial and other information regarding the jointly-owned associated company will normally not be available.

Current Reporting Practices

The review of the published accounting reports of corporations which were co-owners of associated companies revealed a wide variety of methods of reporting this ownership. On one broad point there is general agreement; the accounts of associated companies are not consolidated. The 50% ownership is looked upon as an investment.

But how is this investment shown on the balance sheet? No one method seems to have gained wide acceptance. Main captions such as "Investments," "Investments and Other Receivables" or "Investments and Other Assets" are found in most statements. At times these are followed immediately by the dollar amount, but in most cases the item under consideration is found in a sub-caption.

The contents of these sub-captions reveal a diversity of methods of accounting for the ownership of associ-

ated companies. The many variations make it impossible to give the reader a statistical tabulation that would clearly reflect the scheme of reporting. Instead, three loosely-knit categories will be established and comments made regarding each, preliminary to a brief discussion of some of the important aspects of accounting for this type of investment.

Category 1: No Disclosure. Some companies reveal practically nothing as to the character of their holdings in associated companies. The readers of their reports do not receive a message that even indicates the existence of the "joint-venture" under consideration. The cost of the investment in the associated company is submerged in the investment account with no explanatory comments. Sometimes there is nothing more than the general caption for investments. In other cases the investments in the jointly-owned companies are reported under sub-captions such as "Other" and "Partly-owned Affiliated Companies."

Category 2: Some Disclosure. A second group of companies is more informative. The sub-captions in the investment section of the statements, or related footnotes, indicate the existence of associated companies. Some actually use the title "Associated Companies", while others indicate the percentage of ownership of unconsolidated related companies. Frequently the names of the associated companies are given. This is the largest of the three categories of reporting companies. Information is presented, but its character varies from company to company.

Category 3: Significant Disclosure. The third group includes those companies that provide a significant amount of information pertaining to their 50% owned associated companies. While all companies do not include each item mentioned below, they are liberal in the presentation of data in the financial statements, in notes thereto and in the text of the annual reports.

The data frequently disclosed include: the cost of the investment in specific companies; the name of the associated company; the name of the owner of the other 50% interest; the proportionate equity as derived from the books of the associated company; the current dividends paid by the associated company; the current earnings; the proportionate share of undistributed earnings; and any major commitments inherent in participation in the joint ownership.

Rather than attempt to classify the reports according to the quantity of data presented, it is perhaps better to look at some of the individual points of presentation. The investment is carried at cost in all but a few unusual examples. Here is the basic point of agreement in the statements surveyed. However, a definite problem exists in this area. The cost is often combined with that of other investments, making it impossible to determine the cost of investments in associated companies or in a particular associated company. The limited number of deviations from cost include one example of nominal value of $1 and another in which cost is being amortized by a factor related to the amount of ore being received by a steel mill from an associated ore company.

The equity as shown by the statement of the associated company is of interest to the reader of the statement of the owning company. It becomes especially important if there is a substantial difference between the cost and the equity in the associated company. In addition, such items as the current year's profits, dividends paid and accumulated undistributed earnings pro-

vide a more comprehensive picture of the situation. One problem in connection with much of the data is that it is frequently impossible for the jointly-owned associated company to follow accounting policies that coincide with those of both owners.

The name of the associated company is sometimes presented on the statement or in a footnote; the name of the company participating in the joint ownership is given much less frequently. This information, along with comments regarding the operation of the associated company, is at times found elsewhere in the body of the annual report. More attention is given new ventures than those which have been in existence for several years.

One point found in some examples is the reference to commitments made by the owning companies in connection with the operation of the associated company. Participating companies may agree that each will contribute, as needed, the amount necessary to finance operations of the associated company. An agreement of this type is much more binding than an intention to finance operations of a wholly-owned subsidiary. In other examples, the associated companies borrow by the use of bonds and the owning companies may assume some responsibility in connection with these liabilities.

Suggestions for Better Reporting

The following suggestions regarding accounting for jointly-owned associated companies are made in order to stimulate constructive thinking in this area.

In the light of present accounting practices, the consolidation of the accounts of such associated companies with those of their owners does not seem to be warranted. Present accounting conventions provide for the consolidation of subsidiaries. From a technical viewpoint, the 50% ownership is not sufficient to make a company eligible for accounting consolidation as a subsidiary. From a practical viewpoint there is a good likelihood of a disparity of accounting methods that would make consolidation difficult. It is obviously impossible for the jointly-held company to follow the accounting practices of both its owners.

Unless some drastic change takes place in accounting thought, the ownership interest in the associated company should be carried as an investment. If the amount of this investment is material in comparison with other items on the balance sheet, special attention will have to be given to its presentation. The following paragraphs contain a number of suggestions pertaining to the presentation of the investment in associated companies.

The investment account should be carried at cost. The reporting company would thereby show the amount of its resources which have been actively invested in the associated company. Use of the cost basis would place accounting for this ownership on the same basis as accounting for most other assets.

But how should this cost be presented? It is doubtful if it should be buried in an account where it is commingled with the cost of several other miscellaneous types of investments. For example, investments in unconsolidated foreign subsidiaries should not be combined with investments in associated companies. The cost of investment in a relatively large associated company should be separately disclosed. Less material investments in a number of associated companies could be grouped in one account, but, unless definitely immaterial in amount, should not be

placed in an account with items having a different nature.

Full disclosure of significant information seems to call for the presentation of the equity per the books of the associated company or companies. This should be detailed in the case of major associates, but could well be combined in one figure for minor associates. This equity information becomes especially important when it is realized that the statements of jointly-held associated companies are normally not available for the readers of the owners' reports.

Perhaps some companies would like to make a formal recognition of equity changes on their books. In this special type of investment there may be some arguments favoring it. However, it would appear to be necessary to follow the generally accepted practice where a true parent-subsidiary relationship does not exist, and recognize equity increases only when realized. Such realization would be the payment of cash dividends by the associated company.

Another point of interest is whether a company should indicate that its investment in an associated company is a half ownership of a company, with an equal interest vested in another single company. Inasmuch as this situation differs in many ways from a 50% investment in a company whose remaining stock is publicly held, I believe that the cooperative nature of the investment should be clearly shown. This could be accomplished by caption wording or footnote comment.

Should the name of the participating company also be shown? It does not appear that this question falls in the area of the accountant's responsibility. The disclosure of this information or other items, such as the scope and nature of the associated companies' operations, would seem to be dependent upon management's decision. If desired, this could well be included in the textual material contained in the annual report. As previously stated, some companies make no mention of the existence of the situation while others go so far as to devote a page or more to the associated companies. The start of a new venture of substantial size would surely warrant textual attention, while a continuing situation without new developments would probably not require recognition.

This article has not attempted to prescribe a fixed set of reporting rules to be followed by companies taking part in the joint ownership of associated companies. Instead, it was the writer's intention to provide an informative basis for a further discussion of an important type of corporate relationship which, because of its recent development, has not as yet received sufficient attention in accounting literature.

Appendix

The following tabulations classify, by net worth and industry, seventy-seven companies which have investments in associated companies. The data were developed by the author in his selection of published annual reports for the years 1954 and 1955.

Net Worth (in millions)	Number of Companies
Under $10	7
$10 to $99	34
$100 to $999	28
$1,000 and over	8
Total	77

Industries	
Petroleum	15
General manufacturing	22
Steel and special metals	14
Chemicals	11
Mining and forest products	8
Other activities	7
Total	77

New York State Social Welfare Department Reporting Requirements for Charitable Organizations

By Max Wasser, C.P.A.

This article analyzes the problems faced by the independent public accountant relative to Form CR-131, an annual financial report required to be filed by charitable organizations in the State of New York.

As a result of investigations into the activities of certain charitable organizations, the New York State Legislature in 1954 amended the Social Welfare Law (Laws of 1954, Chapter 418) for the purpose of regulating more closely the operations of charitable organizations. For the first time, charitable organizations soliciting funds in the State of New York were required to file annual financial reports which were to be made available to the public. As a result, prospective contributors can now secure information which may be helpful in evaluating the merits of a particular appeal. The applicable provision of the law is to be found in its section 482-b which states:

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Mr. Wasser is chairman of the Society's Committee on Institutional Accounting, of which he has been a member for a number of years. He has frequently contributed articles to The New York Certified Public Accountant.

> Reports by registered charitable organizations. Every charitable organization required to register pursuant to section four hundred eighty-two of this article which has received contributions during the preceding calendar year shall file a written report with the department upon forms prescribed by it, on or before June thirtieth of each year, which shall include a financial statement covering the preceding fiscal year of operation, verified by an independent public accountant clearly setting forth the gross income, expenses, and net amount inuring to the benefit of the charitable organization. A charitable organization which maintains its books on other than a calendar year basis shall upon application to the department therefor be permitted to file its report within six months after the close of its fiscal year. Such report shall state the names of its professional fund raisers and professional solicitors used during the year, if any, and the amounts of compensation received by them. Such report when filed shall become public records in the office of the department. All records, books and reports maintained by such charitable institutions, shall at all times be available for inspection, at the

principal office of such institution, by the commissioner of social welfare and/or the attorney general, or their duly authorized representatives. (Added L. 1954, C. 418; amended by L. 1955, C. 549)

In January 1955, the Department of Social Welfare, pursuant to the above-quoted law, devised a four-page form, CR-131 "Annual Report—Charitable Organization", pages two and three of which are reproduced as Figures I and II, respectively.

At first glance the report is seemingly simple to complete. The desire to achieve simplicity was apparently the prime motive of its authors. While this is a commendable objective, it was unfortunately done at the expense of accounting principles appropriate to non-profit organizations and therefore resulted in a statement which can be misleading to the public.

Figure I

State of New York — **ANNUAL REPORT - CHARITABLE ORGANIZATION**

Department of Social Welfare — Form CR-131 (Page 2) (Rev. 6/55)

Section B. FINANCIAL STATEMENT - TO BE VERIFIED BY AN INDEPENDENT PUBLIC ACCOUNTANT

PART I. GROSS RECEIPTS AND EXPENDITURES FOR YEAR - ALL PURPOSES

Report below ALL receipts and expenditures of the organization, including operating, capital and any other.

	REPORT ONLY CASH ACTUALLY RECEIVED OR DISBURSED
A. GROSS RECEIPTS	
(1) Earned income (earnings, fees or other payments for services rendered or goods supplied or sold, including dues, admission fees, etc.)	$
(2) Income from investments (interest, dividends, etc.)	
(3) Legacies and bequests - total (For endowment or capital purposes $ ______) (Expendable for current operating purposes $______)	
(4) Allotments received from community chests or other fund-raising and distributing federations	
(5) Receipts from solicitations (same as PART 2, Line A)	
(6) Grants from foundations made on specific application for special purposes	
(7) Other (specify) ______	
(8) Total receipts (sum of items (1) through (7))	$
B. GROSS EXPENDITURES	
(1) Fund-raising expenses (same as PART 2, Line B(6))	$
(2) Salaries and wages, exclusive of those charged to fund-raising, including organization's share of social insurance, retirement fund, etc.	
(3) Other general and operating expenses, including assistance and services rendered by the organization	
(4) Expenditures for capital purposes (see NOTE below)	
(5) This item applies only to community chests, foundations and other fund-raising and distributing federations: Show here total of all funds distributed to member or recipient organizations. Attach CONTINUATION SHEET listing names and addresses of organizations to whom distributed and amounts.	
(6) Total expenditures (sum of items (1) through (5))	$
C. BALANCE (item A(8) minus item B(6))	$

Note: Describe briefly in this space purposes of capital expenditures and amounts thereof.

Objections to Form CR-131

One of the chief objections to the form is that there is no provision for distinguishing the operations of the general funds from special, restricted, building, endowment, and plant funds that a charity may have. There is just no way to combine all receipts and disbursements of a charity in one column, as this report does, and still arrive at a sensible conclusion.

The requirement that the report be on a cash basis is obviously not appropriate for the charitable organization which keeps its books on an accrual basis. It is interesting to note that the law requires the charity to "clearly [set] forth gross income, expenses, and net amount inuring to the benefit of the charitable organization." It would seem that the requirement that Form CR-131 be prepared on a cash basis only, is contrary to the law itself. Furthermore,

Figure II

State of New York — ANNUAL REPORT - CHARITABLE ORGANIZATION

Department of Social Welfare — Form CR-131 (Page 3) (Rev. 6/55)

Section B. FINANCIAL STATEMENT (continued)

PART 2. RECEIPTS AND EXPENDITURES FOR YEAR - SOLICITATIONS

Report below receipts and expenditures for all solicitations, drives, campaigns or other appeals.

	REPORT ONLY CASH ACTUALLY RECEIVED OR DISBURSED
A. AMOUNT OF ALL CONTRIBUTIONS ACTUALLY RECEIVED (see NOTE below)	$
B. EXPENDITURES CHARGEABLE TO FUND-RAISING (include only amounts paid directly by the organization)	
(1) Compensation, exclusive of expenses, paid to professional fund raisers (including their professional solicitors)	$
(2) Expenses of professional fund-raisers (including their professional solicitors) paid by the organization	
(3) Cost of merchandize used to obtain contributions	
(4) Cost of benefits, entertainments, bazaars, etc., sponsored by the organization	
(5) Other direct fund-raising expenses (for example: salaries or portions of salaries of the organization's staff engaged in fund-raising, cost of promotions and advertising, expense of collecting pledges, etc.)	
(6) Total fund-raising costs (sum of items (1) through (5))	$
C. NET AMOUNT INURING TO THE BENEFIT OF THE ORGANIZATION (item A minus item B(6))	$

Note: Include in item A all contributions received, except the amounts reported separately in PART 1 as items A(3) (Legacies and Bequests), item A(4) (Allotments received from community chests or other fund-raising and distributing federations) and item A(6) (Grants from foundations made on specific application for special purposes).

VERIFICATION BY INDEPENDENT PUBLIC ACCOUNTANT

The undersigned ______________________ certifies that he (it) is independently engaged in business as a public accountant with his (its) place of business located at ______________________ ; that he (it) verifies the foregoing financial statement contained in Section B, pages 2 and 3 of this report, to be true and correct in his opinion.

Signature ______________________

Title ______________________

Date Signed ______________

a statement of cash received and disbursed requires the reporting of loans received and repaid as well as other proceeds from the sale or exchange of assets, etc. The inclusion of such transactions in the report, as required, results in a year-end balance which has no relationship to the net income of the organization. Such balance (item "C" of "Part I" of the report) not only has no meaning but can even be misleading to the reader. Since such reports are available to the public, the harm that can result may outweigh the expected benefits of the law.

Further shortcomings of the report are:

1. No provisions are made for contributions in kind.
2. Balance sheets, disclosing the funds held by the organization, are not required.
3. **Depreciation is not acceptable as an item of expense.**
4. **No provision is made for the reconciliation of fund balances.**

"Verification" by Independent Public Accountants

The requirement in the law that the report be *verified* by an independent public accountant was an unfortunate use of a legal term that has no application in the field of accounting. In its legal sense *verification* means an affidavit attached to a petition or pleading, confirming the statements contained therein. The nature of an accountant's engagement generally contemplates the expression of an *opinion* as to the *fairness* with which the statements present the financial condition and operations of the organization.

Figure III

FORM PROPOSED BY SOCIETY'S COMMITTEE

Section B ANNUAL REPORT — CHARITABLE ORGANIZATION Page 2

PART I — FINANCIAL STATEMENT Form CR-131 (1/56)
(Based on method of accounting used by Charitable Organizations)

Accounting method used ☐ Cash ☐ Accrual

A. INCOME AND/OR RECEIPTS:	1. Operating funds	2. Funds for special purposes	3. Building funds	4. Endowment funds	5. Total Cols. 1, 2, 3 and 4
1. Earned income (earnings, fees or other payments for services rendered or goods supplied or sold, including dues, admission fees, etc.)					
2. Income from investments					
3. Net gain or (loss) from sales of investments					
4. Legacies and bequests					
5. Allotments received from community chests or other fund-raising or distributing federations					
6. Receipts from solicitations (same as Part 2, Line A) (Do not include unpaid pledges)					
7. Grants from foundations					
8. Other (specify) ————					
9. ————					
10. ————					
11. Total—(lines 1 through 10)					

Proposed Improvements to Form CR-131

It is no easy task to devise a financial statement form which would be uniformly applicable to all charities regardless of size. The authorities who administer the law, have been well aware of the shortcomings of Form CR-131. They are earnestly endeavoring to improve it. Our Society's Committee on Institutional Accounting has met with them on a number of occasions to discuss certain objections to the form as well as recommendations for improvement. The State authorities have recently submitted a proposed revision of form CR-131 to a number of selected charities and to our Society's Committee for consideration. Some of our proposals have already been reflected in this proposed revision, while others are under consideration. The following are some of the suggested improvements to the form made by our Society, with an indication as to whether they have been incorporated in the proposed revision:

1. In lieu of the one column report on page 2 of Form CR-131, our Society has recommended a multi-column arrangement which is reproduced as Figure III.

Some of the major charities to whom copies of our proposed form were shown, have indicated their approval.

Figure III (Continued)

B. Expenditures and/or disbursements:

12. Fund-raising salaries and expenses ....
13. Public information and education—salaries and expenses ..
14. Cost of assistance and services rendered—Administrative salaries and expenses ....
15. Salaries and wages (not included in items 12 to 14) ..
16. Other expenses (not included in items 12 to 14) (excluding depreciation) ....
17. Depreciation of buildings and equipment (if recorded) ....
18. Capital expenditures (explain on Page 4 or on separate schedule) ....
19. Funds distributed to member or recipient organizations. This item applies only to community chests, foundations, and other fund-raising and distributing federations. Attach continuation sheet listing names and addresses of organizations to whom distributed and amounts.
20. Other (specify) ____________
21. ____________
22. ____________ ______ ______ ______ ______ ______
23. Total—(lines 12 through 22) ______ ______ ______ ______ ______
24. Balance — (item A11 minus item B23) .... ______ ______ ______ ______ ______
25. Balances at beginning of year
26. Balances at end of year .... ====== ====== ====== ====== ======

Note 1—If available append Balance Sheet at end of calendar or fiscal period.

However, the administrative authorities in Albany, are reluctant to accept this recommended form for two reasons. First, they believe it may appear too complex for the reader, and secondly, they fear that the smaller charities may not be able to cope with it. They appear to be ready to accept an abbreviated version of our form as an alternate substitute for page 2 of Form CR-131. This abbreviated version would be a three-column report as follows:

Column 1 — Operating Funds — not Restricted by Donors.

Column 2 — Funds Restricted by Donors.

Column 3 — Total.

2. While the State authorities seem ready to accept either the cash or accrual basis, they insist that "Receipts from solicitations" as well as "Fund-raising salaries and expenses" be reported on a cash basis.
3. Our provision for depreciation is not acceptable to them, but they will not object to a footnote thereon.
4. The fourth suggestion which relates to the accountants "verification" is discussed below.

Verification Section of Report

It was with respect to the verification section of the report that our Society made its major objection. It attempted to have the legislation amended by eliminating the term "verified by an independent public accountant" and substituting the words, "such financial statements shall be accompanied by an opinion signed by an independent public accountant in the form prescribed by the Department."

Unfortunately, all proposed amendments to the Social Welfare Law were not passed in the last legislative session. The Department of Social Welfare is itself recommending a similar amendment for passage in the 1957 session.

Pending the outcome, the Department of Social Welfare cannot accept the deletion of the section "Verification by Independent Public Accountant" from form CR-131. However, the Department has cooperated to the extent that it will permit an accountant to superimpose his opinion over the printed certificate, provided the printed heading "Verification by Independent Public Accountant" remains uncovered. In this connection, the following suggested wording may be used:

> The undersigned .... represents that he (it) is independently engaged in the practice of public accounting and is located at .... and that it has made an independent examination of the financial statements of .... as at ...., in accordance with generally accepted auditing standards. The information contained in Section B, pages 2 and 3 of this report, was reviewed on the basis of such examination and, in the opinion of the undersigned, presents fairly the financial data as required in this report.

Conclusion

As with any new governmental law or regulation, the reporting requirements relative to charitable organizations will undoubtedly undergo modification and refinement. Meanwhile charities and their accountants will have to continue to cope with the problems raised by form CR-131. The State administrative authorities are earnestly doing all within their power to make form CR-131 intelligible and workable. During this interim stage, sincere professional cooperation is required by all concerned to ensure that form CR-131 achieve its basic purpose, within the framework of sound accounting and reporting principles, namely to enable the reader to form reliable accounting judgments with respect to the particular charitable organization.

Federal Income Tax Legislation of 1956

By Samuel A. Dyckman, C.P.A.

This article summarizes federal income tax legislation enacted in 1956. A sequel article by the author will be devoted to 1956 revenue rulings.

During 1956 Congress refined some of the complex and special relief provisions of the 1954 Code, and extended some retroactive relief to transactions under the 1939 Code. No attempt was made to pass a major Revenue Act for the year. The objective was to adjust and extend on an individual basis relief provisions already established. We probably can look to 1957 as the year in which Congress will settle down to a more comprehensive study of the 1954 Code.

The significant 1956 income tax enactments have been briefly summarized below in a manner to show their modifications of existing law.

Samuel A. Dyckman, C.P.A. *and member of the New York Bar, is a member of our Society. He holds the degrees of B.B.A. from The City College of New York and LL.B. and LL.M. (Taxation) from the New York University School of Law. He is a member of Beta Gamma Sigma.*

Mr. Dyckman is presently practicing in the field of taxation. He is an editor of The Journal of Taxation *and also a lecturer on Taxation at the Baruch School of Business and Public Administration, The City College of New York.*

Carryover of Unused Pension Trust Provisions

An acquiring corporation may now carryover the unused pension trust deductions of a wholly-owned subsidiary which it liquidated under section 112 (b)(6) of the 1939 Code. In this limited respect the acquiring corporation becomes entitled to a carryover benefit in the same manner as if the transaction occurred under the 1954 Code. The deduction is available for years beginning after December 31, 1953 and ending after August 16, 1954. *(P.L. 396)*

Extension of Refund Period for Transferee or Fiduciary

An agreement extending the period for assessment of income tax against a transferee or fiduciary, as provided in section 311 (b) (4) of the 1939 Code, now automatically acts to extend the period respecting the credit or refund of such liability. Although this principle had been incorporated previously in section 322 (b) (3) of the same Code, its application was to taxpayers generally. The new amendment is effective as though enacted on August 16, 1954 and applies to taxes imposed under the 1939 Code. *(P.L. 397)*

Limitations on Retirement Income

The 1954 Code grants a limited exemption for retirement income in the form of a tax credit. The maximum retirement income permitted for the credit is $1200. For taxable years beginning after December 31, 1953, but before January 1, 1956, this $1200 amount is to be reduced by tax exempt pension or annuity payments plus earnings in excess of $900 in the case of individuals under age 75. For those taxpayers over age 75, retirement income is not reduced by any earnings irrespective of the amount received. In 1956, two important changes were made effective for taxable years beginning after December 31, 1955. First, the age at which there is no limitation on the amount of earned income has been dropped from 75 to 72 years. Second, the maximum amount that an individual may earn without reducing his retirement income has been raised from $900 to $1200. *(P.L. 398)*

Computation of Credits under Alternative Tax

Corporations computing the alternative tax for taxable years beginning after December 31, 1951 and before January 1, 1954, may now determine the credits for dividends received, for dividends paid, and for a Western Hemisphere trade corporation on the basis of net income without reduction for the excess of the net long-term capital gain over net short-term capital loss. Refunds resulting from this enactment will not bear interest. *(P.L. 399)*

Unlimited Charitable Deductions

Section 120 of the 1939 Code granting an unlimited deduction for charitable contributions has been made to conform with the 1954 Code allowance. The present Code allows the unlimited deduction where, in the current year and in eight of the ten preceding years, contributions plus income taxes exceed 90% of the taxable income. The 1939 Code had allowed such deduction only if the test was met in *all* of the ten prior years. Now, under the 1956 enactment, the "eight out of ten" rule is applicable to all taxable years under both Codes. Any refund available as a result of the new provision will be permitted only if such amount is set aside for charitable purposes. *(P.L. 408)*

Corporate Normal Tax Rate Extended

As originally enacted, the 1954 Code provided for a corporate normal tax rate of 30% for taxable years beginning before April 1, 1955 and a reduced rate of 25% for taxable years beginning after that date. In 1955, the reduction was postponed to April 1, 1956. Early in 1956, the 5% reduction was repudiated once more by an extension of the 30% rate for another year, to April 1, 1957. There has been no change in the 22% surtax rate. *(P.L. 458)*

Capital Gain on Subdivision Sales

Section 1237, a new provision added by the 1954 Code, permits noncorporate investors to realize capital gain on disposition of lots subdivided for sale if the taxpayer makes no substantial improvements on the property materially enhancing its value. Certain enumerated improvements are permitted as "non-substantial" if performed under specified conditions, and if the lot or parcel is held by taxpayer for a period of ten years. The 1956 amendment adds "drainage facilities" to the permissible improvements. It also extends the application of the section to property acquired through the foreclosure of certain liens and to property adjacent to such property, and, in addition, extends

the relief benefits to qualified corporations in the case of land acquired through foreclosure and adjacent property. *(P.L. 495)*

Railroad Reorganization Exchanges

Neither gain nor loss will be recognized in railroad insolvency reorganizations effected after July 31, 1955. This new provision is integrated with the general insolvency rules of section 371 which apply to corporations other than railroads. In conformance with such rules any *boot* received in the reorganization may result in a recognition of gain unless the *boot* is distributed in pursuance of the plan of reorganization. The assumption of a liability by a party to the reorganization will generally not be treated as *boot*. *(P.L. 628)*

Trademark and Trade Name Expenditures

Under existing law, expenditures incurred in connection with trademarks and trade names could not be expensed but had to be capitalized and, since the useful life of such assets is generally of indefinite duration, no amortization was permitted. Beginning after 1955, Congress eliminated this restriction by permitting expenditures directly connected with the acquisition, protection, expansion, registration or defense of a trademark or trade name to be amortized over a minimum period of 60 months. The election does not apply to the purchase of existing trademarks or trade names. *(P.L. 629)*

Livestock Sold Because of Drought

Section 1033 of the 1954 Code permits taxpayers to defer realized income on the sale or destruction of diseased cattle by making timely replacements. The new amendment includes within the definition of *involuntary conversion* the sale of livestock, (draft, breeding and dairy) other than poultry, sold or exchanged after 1955 solely on account of drought. A drought is defined as a condition in an area by reason of abnormally low precipitation. *(P.L. 629)*

Corporate Distributions of Appreciated Property

In *Hirshon* and *Godley* the courts held the full value of a property distribution under the 1939 Code taxable as a dividend if there were sufficient earnings and profits to cover the adjusted basis of such property. The fact that the earnings and profits were less than the value of the property was ruled immaterial. Regulations promulgated under the 1954 Code overruled these cases by making a property distribution taxable only to the extent of the corporate surplus. The 1939 Code has now been amended retroactively to apply that rule to all years open under the 1939 Code. *(P.L. 629)*

Undistributed Gains of Regulated Invested Companies

A shareholder of a regulated investment company has been granted special tax relief beginning January 1, 1957 with respect to the undistributed capital gains. He must include such undistributed gains in his income, but is deemed to have paid his share of the 25% tax imposed on the corporation which amount can then be claimed as a credit or refund. The basis of his shares is increased by 75% of the undistributed gain required to be included in his long-term capital gains. *(P.L. 700)*

Medical Research Organization Constitutes a Hospital

A special charitable deduction for individuals limited to 10% of adjusted

gross income is available in addition to the maximum 20% deduction, where the extra 10% is made to churches, schools, or hospitals. A hospital was defined as not to include medical research organizations. Effective for taxable years beginning January 1, 1956, such organizations are treated as hospitals for purposes of the 10% limitation, provided the organization is committed to spend the contribution for active research in conjunction with a hospital within five years. *(P.L. 1022)*

Sale of Patents Under 1939 Code

The 1954 Code permits inventors to treat the profit on sale of a patent as capital gain even though the payments received consists of *royalties.* An identical provision has been added to the 1939 Code applicable to amounts received in any taxable year ending after May 31, 1950. *(P.L. 629)*

Claims Against the United States

Section 106 of the 1939 Code limited the surtax on individuals to 30% in the case of amounts received under a claim against the United States involving the acquisition of property, and remaining unpaid for more than 15 years. Application of this maximum 30% rate has been extended to payments received from the United States, prior to January 1, 1950 under a claim arising "for the construction of installations or facilities for any branch of the armed services of the United States and remaining unpaid for more than 5 years". *(P.L. 629)*

Life Insurance and Bank Holding Companies

Congress also passed three acts of limited application, continuing the basic formula with modifications for taxing life insurance companies that was first enacted in the Revenue Act of 1942, and permitting a program of tax free divestments of property by a bank holding company. *(P.L. 429, P.L. 784, P.L. 511)*

Travel and Entertainment Expense

By JACK SCHLOSSER, C.P.A.

In this article, the author discusses and comments on the current status of the deductibility of travel and entertainment expense as reflected in three recently issued pronouncements: *Internal Revenue Service Publication No. 300; Revenue Ruling 56-168;* and a special instruction to revenue agents.

Internal Revenue Service Publication No. 300

During April 1956, the Internal Revenue Service issued the above-cited publication under the title "Deductions for Travel and Transportation Expenses". While it ranges over a broad area, it is principally concerned with that classification of expense known as "travel expense while away from home". This class of expense is significant, not only because it includes a number of items which may be deducted in arriving at *net taxable income,* but because it represents a group of expenditures which may be deducted in arriving at *adjusted gross income.* The significance of this distinction is easily recognized. If deductible in arriving at adjusted gross income, such expenses may be deducted along with the standard deduction. They would have the effect of increasing available medical deductions. They would also play a part in determining the maximum charitable contribution deduction.

This classification of expense has one other significance to taxpayers and their representatives. When the taxpayer is "away from home", his deductible expenses include meals and lodgings. This is the only situation where these clearly personal expenses qualify for tax deduction.

Items Deductible as *Travel Expense*

The *Publication* first discusses those items which may be included under the classification of "Travel Expense" which it associates with being "away from home." For example, it will include fares, baggage charges, meals and lodging, and tips incidental to any of the foregoing. It will not include laundry and cleaning expenses while "away from home". Presumably such expenses retain their personal nature even though incurred and paid for during the course of a business trip. Gifts and entertainment expenses do not fall into the travel expense category, even though incurred and paid for while "away from home".

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This article is an expanded version of a paper presented by Mr. Schlosser at the Society's general meeting held on October 3, 1956.

This, of course, does not mean that gifts and entertaining expenses may not be a proper deduction. It merely signifies that it may not be included in the classification of "travel expenses away from home". Such expenses, if deductible, may not be deducted in arriving at adjusted gross income. Furthermore, gifts and entertainment expense may be deductible even if incurred when the taxpayer is not "away from home".

What Constitutes the Taxpayer's Home?

The foregoing discussion indicates that an expense falls into the "travel expense" classification only if the taxpayer is "away from home". It is therefore necessary to establish what is meant by "home" for this purpose. The taxpayer's home is his principal place of business or employment. This is not restricted merely to the immediate town or city but will usually include the homogeneous general area in which this site is located. It will generally include the suburbs and may even extend further. In New York City it would probably cover not only the immediate suburbs of Westchester and Long Island but would probably include the section we commonly refer to as the Greater New York Metropolitan area, and would certainly take in Jersey City, Newark and the surrounding vicinity.

It is clear that the taxpayer's home need not necessarily be where his principal residence is located or where his family resides. If the taxpayer has a permanent position in Albany but his family is located in New York City, his residence will be the latter but Albany will constitute his home for tax purposes.

A taxpayer can have two places of business or employment but only one will generally be his tax home. As a rule, his principal place of business or employment will constitute his home. This determination, as to what constitutes the principal place of business or employment, in most cases will be fairly obvious. It will be made on the basis of time spent at each location, compensation derived from each location and/or the importance of the duties performed at each location. The only time that this issue may prove troublesome is when there is a sharp disparity in the foregoing factors. For example, if the taxpayer spends less time at one location but earns most of his income therefrom, that particular location may be deemed his home. On the other hand, the element of time may be the determining factor even though the earned income is not proportionate to time. The courts are in conflict on this particular issue.[1] Generally speaking, this should not present great difficulties. Where the taxpayer has two such places of business or employment, his stay at the subsidiary post of duty must be temporary in nature and not indefinite. If it does not satisfy this requirement, it will become his new tax home.

We have noted that a visit to a new post of duty must be temporary if taxpayer is to be deemed "away from home". It therefore becomes important to distinguish between temporary visits and indefinite stays. The point of distinction seems to be whether or not the termination of the visit can be foreseen in the near future with reasonable definiteness. If the termination of the tour of duty is reasonably foreseeable, then the stay is temporary, the job site does not become "home" and the taxpayer's expenses at said job site (including meals and lodging) constitute "travel expense while away from home". If the stay is indefinite in nature then the job site qualifies as taxpayer's tax "home".

Away from Home Overnight

Publication No. 300 points out that taxpayer's expenses of a business trip will not fall into the travel expense category merely because the taxpayer is *away* from home. He must be away from home on an *overnight* basis. This is an administrative view adopted by the Internal Revenue Service without mention in the law and has been disputed on several occasions by the courts.[2] Nevertheless, the Department indicates that this overnight status will not be attained unless the length of duty exceeds a normal work day and requires relief from duty to obtain sleep. The *Publication* itself is quite specific. The work activity must be interrupted not merely to obtain *rest* or a *meal*, but for the purpose of obtaining *sleep*.

Commutation Expenses

Commutation expenses are personal expenses and, hence, may not be deducted. Nor does it matter, in most cases, whether the taxpayer is "home" or "away from home". Distance between taxpayer's residence and his job site or the length of time required to traverse that distance will not change this rule, nor will it be altered by the cost of said transportation. The number of places of business or employment will not affect the outcome. The initial expense of traveling from taxpayer's residence to his first job site of each day, and the similar expense of returning home from his last work location will not be deductible as commuter expense. Any other expenses of traveling from job site to job site during the course of the day will be deductible.

There are apparently two exceptions to this otherwise quite specific rule. If the taxpayer is *away from home* and the nearest acceptable living quarters is 10 miles or more from the job site, *Publication No. 300* indicates that such expenses will not be deemed personal commutation expenses. If the taxpayer's job site is temporary or minor in nature and is located outside of his general home area, the expenses of traveling to that job site from his residence will be deductible.

Other Features

A considerable portion of *Publication No. 300* is devoted to a series of questions and answers related to this general topic, some of which are of fairly widespread significance. For example, it is pointed out that expenses incurred in attending courses to obtain a position, attain a higher position, secure permanent status or satisfy general cultural aims may not be deducted. The courts have already made it clear that a professional man may deduct the expenses of attending a series of lectures calculated to maintain his technical skills.[3] They have also indicated that a teacher may deduct such expenses when the course of study was necessary to maintain his existing position.[4] In addition, the *Publication* points out that a taxpayer (accountants included presumably) may maintain a position in New York City for eight months of the year and a temporary position in Florida for four months. Assuming that said taxpayer maintains his residence throughout the period, it would appear that New York City constituted said taxpayer's "home" and he would be eligible to deduct all of his Florida expenses, including fares, meals, lodgings, etc.

There are many other points of specific interest discussed in this question and answer section of the *Publication* which are worthy of more than passing scrutiny.

Revenue Ruling 56-168; IRB 1956-17

Combination Business and Personal Trips

This ruling, also issued during April 1956, represents the Treasury Department's answer to a series of problems

growing out of the practice of taking business trips, including trips to business conventions, by taxpayers together with members of the family, and especially where opportunities for vacationing are present. The issue faced by the Service was the determination of the nature and deductibility of these expenses. Out of this ruling emerged certain specific rules:

1. Where a trip is primarily for business purposes, and the vacationing or socializing aspects are minor and incidental, taxpayer may apportion his costs and deduct the business portion thereof.
2. Where the trip is essentially for personal purposes, no deduction for any portion of said expenses will be allowed even though it is established that incidental business functions are performed.
3. The expenses of members of the family who accompany the taxpayer, may not be deducted unless it is established that their presence is for direct business purposes. Where a wife performs incidental functions having business value, such as answering telephones, writing letters or attending social functions, such activities will not permit the deductibility of even an allocable portion of her expenses.

Personal Expenses Incurred for Business Reasons

There is a question as to whether the Treasury Department's strict view of personal trips with incidental business activities can be supported in the courts. It may well be that the burden of proof as to the business aspect of the trip may be more burdensome in these cases, and the approach of the courts in making apportionments may be severe, but it seems extremely doubtful that the Service is correct in holding that absolutely no portion of such costs is deductible.

It would appear that this view is an outgrowth of a gradually tightening approach to the deductibility of personal expenses incurred during the course of business activities. For example, it has been held that a taxpayer may not include the cost of his own lunch even though incurred during the course of entertaining business associates for business purposes.[5] In addition, it has recently been held that the costs attributable to a partner's meals and lodging may not be deducted in arriving at the net income of the partnership operating a hotel, even where it is established that his presence is necessary.[6]

Notwithstanding these cases, the Treasury Department's view with regard to the total non-deductibility of expenses of a trip having incidental business purposes does not appear to be comparable since there is a specific holding that meals and lodging are deductible (despite their primarily personal nature) when incurred away from home.

Recent Examination Developments

Now being experienced are the aftereffects of a recently issued instruction to Revenue Agents in the three New York City Districts with regard to corporate business expenses, especially in the case of closely-held corporations. This instruction may be divided into three segments.

Joint Examinations

Where corporate expenses are being considered for disallowance on the ground of lack of substantiation or because they are personal in nature, it is urged that Revenue Agents make simultaneous examinations of the tax returns of stockholders, principal employees, affiliated corporations or partnerships, etc. Ostensibly, the purpose for this procedure is to follow up the proper treatment of expense reimbursements and to prevent duplicate deduc-

tion of expense. Furthermore, it would facilitate any attempt by the Service to tax the recipient a part or all of the disallowed expense.

Personal Expenses

Revenue Agents have been instructed to approach with greater firmness the question of corporate expenses which are personal in nature. Special attention is to be paid to golf club expenses, auto expenses, boat expenses, etc.

However, the examining officer is not to be content with a disallowance of that portion of expenses deemed to be personal in nature. Where the character of the expense is clearly established as personal, it is to be taxed to the individual or individuals receiving the benefit of such expenditures. It is obvious that the effect of this procedure is to treat the expenditures as the equivalent of cash dividends. In the case of individuals in high brackets, it is quite possible that the aggregate corporation and individual deficiency may be greater than the disallowance itself. There seems to be little defense against taxing these items to the individual beneficiaries. However, practitioners should consider the possibility of contending that such expenses, even if personal in nature, can still be deductible by the corporation on the theory that they represent additional compensation. This procedure will at least make for only one deficiency. However, it will be necessary, in such instances, to establish that the aggregate compensation, including these expenses, is reasonable in amount.

Cash Expenditures

Special attention is to be devoted to cases of substantial cash expenditures which are deducted as corporate expenses. Included in this category would be expense checks drawn to the order of stockholder-employees or payable to cash. In addition to determining whether any portion thereof is disallowable on the grounds of lack of substantiation, the examining officer is to give serious consideration to taxing these amounts to said stockholder-employees. Here the Treasury Department is not on firm ground and may be aware of this. While no definitive procedural rules have been laid down with regard to this problem, several group chiefs and reviewers have presumably indicated that Revenue Agents are to review the personal bank accounts of stockholder - employees to determine whether any of the expenses in question have been deposited therein. In addition, they are to examine the known sources of living expenses. If it can be established that some of these cash expenditures ended up in the taxpayer's bank account, or if he is unable to account for his standard of living, then it would be deemed that a basis had been established for including some part or all of the disallowed cash expenses in taxpayer's taxable income. Whether this procedure is sufficient to sustain taxability will remain to be seen.

There can be little doubt that the handling of tax examinations in the case of closely-held family corporations will be considerably more difficult for some time to come until all of the problems raised by these recent instructions have been clarified and examination procedures are standardized.

References

1. *Joseph H. Sherman*, 16 TC 332, 1951, Acq.; *Helen E. Stairwalt*, TC Memo Decision, 1952; *Vincent Treanor*, TC Memo Decision, 1951.
2. *Kenneth Waters*, 12 TC 414, 1949; *Scott* v *Kelm*, DC, Minn., 1953; *Horace E. Podems*, 24 TC No. 3, 1955.
3. *Coughlin* v *Comm.*, 2 Cir., 1953.
4. *Hill* v *Comm.*, 4 Cir., 1950.
5. *Richard A. Sutter*, 21 TC 170, 1953.
6. *Everett Doak*, 4 Cir., 1956.

Stock Redemptions—Some Current Aspects

By Samuel Mirandy, C.P.A.

Discussion of a few current developments in the area involving shareholders' efforts to raise cash through stock redemptions.

How Redemption Problem Arises

Although sales of stock to outside interests will generally produce automatic capital gain treatment, such sales are not customary in the case of the prosperous, closely-held corporation, because of reluctance to bring new ownership into a successful business, or the difficulty in agreeing upon a fair value for the stock, or because of the prospective purchaser's insistence upon acquiring all, rather than a portion, of the outstanding shares. Under these circumstances transfer of stock to the corporation is the easiest and most convenient method for the shareholder to raise capital.

This constitutes a redemption. A redemption takes place, for tax purposes, whenever a corporation acquires its stock in exchange for property.

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Since the person surrendering the shares, or his family or other related interest, often continues to retain some stock interest in the corporation after the redemption, the question of dividend treatment, as opposed to capital gain treatment, comes into immediate focus. Satisfying the Service that the distribution was not essentially equivalent to a dividend has proved most difficult, except in the most meritorious instances.

1954 Code Amendments

This area of uncertainty with respect to classifying redemption payments caused Congress to introduce two definite standards in the 1954 Code either of which, if met, would permit the taxpayer to treat the payments as consideration in exchange for stock, rather than dividends.

The first test, referred to as the substantially disproportionate redemption, is met if the surrendering shareholder experiences, as a result of the redemption, a dilution of more than 20 per cent in the ratio of his holdings of voting stock as well as common stock of the corporation, provided, furthermore, that such shareholder does not continue to hold 50 per cent of the voting power. The second test is met if the redemption results in a complete termination of interest as a stockholder in the corporation.

Although the dividend problem is seemingly eliminated where the factual pattern fits either of the aforementioned mechanical tests, the taxpayer should be cautioned as to the necessity of satisfying the constructive stock ownership features which are so closely interlocked in the application of the new provisions.

The rules under which ownership of stock held by other persons is attributed to the surrendering shareholder extend, in either direction, to such areas as members of the family (excluding brothers and sisters), partnerships, estates, certain trusts in which the taxpayer is a beneficiary or a grantor under circumstances where he is considered the owner of the trust, as well as any corporation in which the person owns 50 per cent or more of the value of the stock. Family attribution rules are waived upon compliance with specified conditions if qualification relates to the complete termination of interest rule.

Some Recent Developments

During the past year regulations pertaining to corporate distributions were finalized, almost one year after they were introduced. Needless to say, they evoked almost as much criticism in their final form as when first introduced. A considerable portion of the objections has been directed towards the constructive ownership rules, the rules for policing the termination of interest provisions where family attribution rules are to be waived, and the "vanishing basis" in transactions where the redemption of all the taxpayer's shares is, because of the ownership attribution rules, taxed as a dividend.

Despite the absence of significant court decisions dealing with stock redemption provisions of the new Code the current position of the Service with respect to the *Zenz* rule may be of interest. Within the past year the Service has indicated (Rev. Rul. 55-745) that a disposition under facts and circumstances similar to *Zenz* will be treated as payment for stock under the termination of stockholder's interest rule in the 1954 Code.

The 6th Circuit Court reversed the District Court in 1954 so as to permit capital gain treatment to Mrs. Zenz who had surrendered all of her shares in a corporation with substantial accumulated earnings. Under a plan admittedly carried out for the purpose of avoiding taxes, this sole stockholder sold a fraction of her stock interest in a corporation to an outside party and, three weeks later, surrendered the balance of her shares to the corporation for redemption. The Service had contended originally that the two transactions were inseparable and that the redemption served no purpose other than to syphon earnings and profits which should be taxed as a dividend.

The Service's present position is particularly beneficial in those instances where the owner is unable to negotiate a satisfactory deal for the transfer of his entire business or where he may prefer to sell to key employees who, however, are unable to finance the purchase of all the outstanding shares. Selling a portion of the shares to the key employees and redeeming the balance would achieve the objective desired. Considerable interest in this form of redemption will stem from the fact that the Service will issue an advance ruling.

The Service has issued during the past year a series of rulings serving to clarify or highlight the significance of the constructive stock ownership rules. Accountants rendering services to the principal stockholders of closely-held corporations will attach unusual significance to Revenue Ruling 56-103 in which the Service held that a redemption

by an estate, pursuant to the terms of a buy-sell agreement covering the stock of a closely-held corporation, was taxable as a dividend. The decedent in this situation had owned 27 per cent of the corporate stock. His son, who was beneficiary of his estate, owned 48 per cent and the remaining shares were owned by unrelated employees. The corporation acquired all of the decedent's stock from his estate at a formula price established under a buy-sell agreement.

The estate could not qualify under either the substantially disproportionate redemption rule or the complete termination of interest rule because it was deemed in this instance to own all of the son's stock. The attribution rules provide that stock owned by the beneficiary of an estate shall be considered as owned by the estate. The ruling also held that the distribution was essentially equivalent to a dividend on the grounds that the relative stock interest of the principal stockholder was not materially changed by the redemption. The new regulations provide, contrary to the express language of the Committee Reports, that constructive stock ownership rules will apply to all redemptions including those which seek to qualify as exchanges on the grounds that the distribution was not essentially equivalent to a dividend.

The position of the Service in this ruling has a far-reaching effect. Parties to buy-sell agreements are forewarned to carefully review their agreements and take steps, where necessary, to make certain that the future redemption will qualify as a capital gain. The executor of the future estate may otherwise be confronted with a most perplexing situation upon discovering that an immediate stock redemption, which may be either desirable financially in the opinion of the executor or compulsory due to the insistence of the other stockholders, will result in a huge dividend tax.

Under the rationale of the above ruling, dividend treatment would presumably apply to a corollary situation where a substantial stockholder of the corporation has more than a contingent interest in a trust holding stock in the same corporation. Should the trustees decide to diversify and surrender for redemption all, or any portion, of such stock the trust would be required to treat the proceeds as dividend.

Redemption of 306 Stock

No discussion of stock redemptions would be complete without some reference to the "hot" or "tainted" stock known as "section 306 stock." Generally speaking "section 306 stock" is preferred stock issued after June 22, 1954 as a stock dividend at a time when the issuing corporation has earnings or profits. The substantially disproportionate rules set forth under Sec. 302 do not apply where redeemed stock is "section 306 stock."

Payments received in redemption of "306 stock" will be treated as dividend income in amounts not exceeding the earnings and profits at *time of redemption* unless it can be established that tax avoidance was not the principal purpose of the distribution and redemption. A non-tax-avoidance situation would presumably exist in the case of a minority stockholder who had no voice in the distribution or redemption. Exception to the dividend treatment is made where there is a complete termination of interest, in which event the transaction results in capital gain. The "section 306 taint" is removed from the previously distributed shares upon death of the owner.

Some Basic Precautions

Prorata redemptions of voting stock are obviously dividend distributions and should be avoided wherever possible. Neither of the two new mechanical tests, substantially disproportionate redemption or complete termination of stock interest, could possibly apply.

Retention of identical common stock interests by the heirs of a decedent may be simplified where the "section 306 stock" is distributed during his lifetime in an amount approximately sufficient to liquidate the estate tax liability and the administrative expenses of the future estate. Although such shares could be distributed to the estate after death and still qualify for capital gain under the distributions in redemption of stock to pay death taxes features of the present law, the desired retention of control might be more effectively achieved when engineered by the important stockholder during his lifetime.

Stock redemptions are often necessary because the estate must raise cash to pay death taxes. Adequate capital gain opportunities are extended to such redemptions where the value of the stock investment in such corporation held by the decedent exceeds either 35 per cent of the gross estate or 50 per cent of the taxable estate. The constructive stock ownership rules do not apply to redemptions of this type. Persons anticipating that their estates may seek the advantages of this extremely favorable redemption feature, should instruct their accountant to prepare periodic, at least annual, net worth statements. Ascertainment of net worth is required inasmuch as fair market value at death will control for this purpose. The acquisition or disposition of assets plus constantly fluctuating values may cause sudden shifts in the eligibility status. If necessary to insure qualification, the stockholder should either increase the stock investment in this corporation or make lifetime gifts.

Standards of Education and Experience For CPAs

I—The Undergraduate Accounting Program

By DANIEL LIPSKY, C.P.A.

This article is the first in a serial discussion and analysis of the Report of the Commission on Standards of Education and Experience for Certified Public Accountants. The author takes the position that *professional* C.P.A. training properly begins on the undergraduate level and should not be confined to the proposed graduate program.

A new approach to preparation for the certified public accountancy profession is exhibited in the long-range recommendations of the Commission on Standards of Education and Experience for Certified Public Accountants. The Commission's report places the predominant emphasis upon formal education for preparation of candidates for the profession, and anticipates the elimination of experience as a condition for the award of the CPA certificate. It is appropriate, therefore, that any appraisal of the recommendations should start with a consideration of the undergraduate academic program.

A brief review of the long-range goals will help in visualizing the place of undergraduate studies in the total program. At the outset, the prospective CPA is expected to complete a four-year college program including a major in accounting. This is to be followed by a postgraduate professional academic program. An internship of approximately three months is to be included in the postgraduate work. A qualifying examination is proposed upon completion of the undergraduate program to assist in evaluating and selecting students who wish to pursue the required postgraduate academic training. College graduates who have specialized in other fields, such as arts, science, or engineering are expected to complete the equiva-

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lent of the accounting major as a supplement to their undergraduate work before undertaking the professional program.[1].

The Undergraduate Curriculum

What is to be the composition of the undergraduate academic program? The Commission suggests the nature of the liberal arts content by referring to the report of the Standards Rating Committee of the American Accounting Association.[2] This report is of interest not only for its cultural prescription but also for its description of the curriculum content of an undergraduate accounting program. The curriculum pattern rests upon the theory that education for the professional accountant should embrace three ultimate objectives: Education for citizenship, education in business and education in accounting.

To meet these objectives, the Standards Rating Committee apportions the four-year undergraduate program as follows:[3]

1. *Liberal, cultural, and general nonbusiness studies,* approximately 50% of the program, including courses in written and oral communication, humanities, natural and social sciences, and such other areas as mathematics, engineering and agriculture.
2. *General business studies,* approximately 25% of the program including courses in marketing, production, finance, industrial relations, business law and statistics.
3. *Accounting studies,* approximately 25% of the program, including courses in accounting principles (elementary, intermediate and advanced), cost accounting and cost analysis, auditing principles and procedures, problems of income tax accounting, as well as possible optional courses in budgeting, systems, and governmental and institutional accounting.

The foregoing curriculum is essentially in accordance with current CPA educational requirements in the State of New York. It would also appear to fulfill the educational requirements contemplated by the Commission for the transitional stage. The long-range goal presumably contemplates that the undergraduate curriculum will be modified to provide for an increase in the liberal arts and cultural content and for a shifting of some of the business and accounting studies to the postgraduate period.[4] The emphasis by the Commission on a *professional* academic program, entirely appropriate when considered on a nationwide basis, does not have the same significance in states which have already made substantial progress in achieving a professional orientation on the undergraduate level.

Liberal Arts Content

The provision for additional liberal arts study, when viewed in the light of the proposed general increase in educational requirements, can hardly bring dissent. It is important that the professional man should not confine his training to purely professional and technical areas. To quote Donald P. Perry in his Dickinson lectures:

> "Extensive familiarity with history, literature, and philosophy will humble the specialist's attitude and lead him to understand his calling against the broad background of historical development and of the cultural inheritance of society. The revelations of the liberal arts are conducive of flexibility of mind and a wider comprehension of a whole array of problems and situations in life, so that a man becomes better fitted and more confident to deal with new situations which he will surely encounter."[5]

It is difficult to specify the courses which should be added to the liberal

arts portion of the undergraduate curriculum. Perhaps all that is needed is merely more of what is already there. On the other hand, some educators will undoubtedly urge a restoration of foreign language study. Schools of business generally have a lower requirement in that respect than colleges of liberal arts and science. There is also likely to be pressure to increase studies in what may be considered to be peripheral business subjects. The degree of emphasis to be placed on written and oral communication depends on what is to be accomplished in the high schools and how much is to remain for the postgraduate program. There can be no fixed prescription for a liberal arts and cultural base.

The Undergraduate Accounting Major

The undergraduate college curriculum, even with an extension of liberal arts and cultural content, is still to retain a major in accounting. Accounting educators would certainly agree that the progressive sequence pattern of accounting study makes it desirable to retain a substantial undergraduate accounting major. The Commission makes no attempt to specify the undergraduate major. In general, it would be expected to include basic courses in accounting and auditing principles as well as commercial law and related courses in business administration.[6]

The remainder of this article is devoted to a consideration of the following three aspects of accounting education which have relevance to undergraduate studies.

1. The professional aspect of the undergraduate program.

2. Ethics and standards of professional conduct.

3. Courses in auditing.

The Professional Aspect of the Undergraduate Program

The Commission recommends "the development of a type of curriculum which would be new in accounting but has been tested for generations in other professions — a professional program, with classroom materials drawn from public practice, with faculties experienced in public accountancy and maintaining close contact with changes in that profession, and with students directly and specifically interested in preparing for a career in public accountancy as a CPA."[7]

Although thus described as a new type of curriculum, this professional program, in many of its aspects, is currently being carried out on the undergraduate level in a number of colleges and schools of business.[8] In these colleges the faculties, for the most part, are CPAs; they do keep abreast of changes in the profession; many combine teaching with public practice. The alert instructor constantly brings into the classroom the situations he finds in practice. This is true not merely in advanced courses but also at the elementary levels. In this constant relating of classroom theory to actual practice, and to the needs of business and government, accounting becomes live and significant to the student. And this is also beneficial to the non-accounting major who shares the elementary courses with the accounting major.

The students preparing for the CPA profession in these schools are directed through specific, progressive and integrated courses of study. As is to be expected, in the advanced courses the enrollment consists almost entirely of students planning careers in public accounting. Even with reduced accounting work at the undergraduate level, there is no reason why an accounting major

should not be imbued with a professional approach as soon as he starts studying accounting.

Professional Conduct

In its recommendation for a postgraduate professional academic program, the Commission makes note of the fact that standards of professional conduct receive "little attention in the usual undergraduate program."[9] Instruction in professional ethics cannot be confined to a single course, nor should it be limited to a postgraduate program. The inculcation of ethical thinking and an awareness and understanding of the accepted standards of professional conduct are elements to be considered in all courses in the accounting curriculum. In a professionally conceived and integrated academic program, each instructor will find or create occasions to relate the major subject matter of the course to concepts of ethical practice. Concepts of independence and objectivity should be introduced as early as the elementary course in accounting. For the non-accounting major, this emphasis on ethical principles adds to the cultural value of an accounting course. For the prospective CPA, it may be identified with professional training.

Courses in Auditing

The Commission believes that "college courses in auditing are subject to more criticism, by educators and practitioners, than any other part of the accounting curriculum." The chief criticism is that insufficient time is devoted to the development of the subject.[10]

The lack of time, in the opinion of the writer, is due chiefly to two factors. The first is that the undergraduate program, itself, is limited in time. In view of the already restricted liberal arts content of the standard undergraduate program, additional time for an auditing course can probably be found only by discarding some of the optional accounting specialties.

The second reason for lack of time is the loading of course content in auditing. The auditing course often is expected to serve as a capstone to the entire undergraduate accounting curriculum. As such, it is called upon to provide a substantial review of accounting theory and to include considerable material on the administration of an accounting practice. The auditing course should presume a knowledge of accounting theory just as an accounting course presumes a knowledge of business mathematics.

The auditing course in the undergraduate curriculum can furnish a firmer foundation for the future practitioner if the fringes are removed and its content is limited to the more essential study of auditing principles and standards.

Conclusion

The Commission's educational recommendations call for an extension of training in both technical accounting and the liberal arts. On the postgraduate level the technical training is to be established along *professional* lines. However, it would seem entirely appropriate for the professional approach to begin in the undergraduate course of study so that a firm foundation may be established to facilitate the transition to the graduate program.

Many institutions have already achieved such a professional orientation in the undergraduate program. The Commission's emphasis upon graduate professional training should not be allowed to detract from continuing efforts to strengthen the professional character of undergraduate accounting studies.

References

1. *Standards of Education and Experience for Certified Public Accountants,* University of Michigan, 1956, p. 128.
2. *Ibid.*
3. "Report of Standards Rating Committee of the American Accounting Association," *The Accounting Review,* January, 1954.
4. The Commission states it "has not attempted to specify either the content or the proportion of the four-year undergraduate program which should be devoted to general and cultural areas of study, although the recommendations of the Standards Rating Committee of the American Accounting Association, and the requirements of the American Association of Collegiate Schools of Business, are considered realistic and satisfactory *minimum* standards under *current* conditions. The Commission also recognizes the great value of an undergraduate curriculum, *concerned principally with cultural and 'liberal' subjects,* for those students who can afford the necessary time and expense before undertaking professional study." [Italics supplied.] *Standards of Education and Experience, op. cit.,* p. 128.
5. Donald P. Perry, *Public Accounting Practice and Accounting Education,* Harvard University, 1955, p. 52.
6. "It is anticipated that the accounting curricula at the undergraduate level could be restricted to basic courses in principles. . . ." Also, in connection with graduates who major in other fields, ". . . the equivalent of an accounting major (including accounting, auditing, commercial law, and related courses in business administration) . . .," *Standards of Education and Experience, op. cit.,* p. 130 and p. 128.
7. *Standards of Education and Experience, op. cit.,* p. 130.
8. In a sense the Commission acknowledges this. See p. 48: "There are some (schools of business administration) which purport to offer 'professional' programs. . . ." Note also the footnote on the same page which acknowledges the exception: "An exception to this generalization should be made for a few educational institutions which maintain careful, periodic checks on the academic progress of students in the 'professional' program. Some of these institutions graduate highly qualified individuals with substantial professional training." *Standards of Education and Experience, op. cit.*
9. *Ibid.,* p. 132.
10. *Ibid.,* p. 55.

THE COLLEGE TEACHER OF ACCOUNTING

It is my opinion that the successful college teacher of accounting must be more than a competent professional specialist constantly in contact with the theory and practice in his field. He must have common cultural bonds with other educated persons. He must also possess the rare ability to teach, and thus facilitate the student's absorption of information, knowledge, principles and relationships as well as his acquisition of skills, attitudes, interests and ideals. He must be sufficiently alert and stimulating to pace the bright student, as well as patient and understanding enough to encourage the stragglers. That is not an easy order to fill these days, particularly in the light of the attractive offers which such men are known to receive from other sources.

The college teachers of accounting are on a threshold of an era that offers them the greatest challenge since the beginnings of our profession. Let us hope that our thinking, our planning and our actions are all equal to the opportunity that now confronts us!

"Some Thoughts on Education for Public Accountancy" by Dr. Emanuel Saxe, The New York Certified Public Accountant, November, 1946.

New York State Tax Forum

Conducted by Benjamin Harrow, C.P.A.

Change of Classification—Additional Tax . . . The Term Resident Under the Income Tax Law.

Change of Classification—Additional Tax

If a real estate corporation becomes taxable as a business corporation it must pay an additional tax of 2% on the amount of its surplus at the time of such change of classification. The underlying theory of this provision is that when a real estate corporation becomes taxable under another section, all of the surplus that would have been taxable if distributed while the corporation was taxable as a real estate company, should immediately be taxed so that the state will not lose the potential revenue it might derive from the undistributed surplus.

Benjamin Harrow, C.P.A., *has been a member of our Society since 1928, and a member of the American Institute of Accountants since 1922. He is a member of the New York Bar and Professor of Law at St. John's University.*

Mr. Harrow is a past Vice-President of the Society. He is a member of the Society's Committees on Meetings and Committee Operations, and has served for a number of years on the Institute's Committee on Federal Taxation.

Mr. Harrow is engaged in practice as a certified public accountant and attorney in his own office in New York City.

One of our members calls our attention to the provision in Section 3 of Article 16 of the New York State Constitution which prohibits the taxation of undistributed profits. Is not this provision applicable to the additional tax of 2% of the surplus of a corporation at the time of a change of classification? The issue has never been decided by the courts. Under the plain language in the Constitution it is true that the profits are not actually distributed. The Tax Commission would probably argue that the surplus is deemed to be distributed by the Article 9 corporation to itself as an Article 9A corporation. Whether courts would accept this reasoning in order to protect a potential loss of revenue is an unknown question which should be submitted to them.

It should also be noted that the provision with respect to the taxation of undistributed profits was put into the Constitution in 1939. It was probably not intended to apply to the additional tax of 2% since the latter had been in effect long prior to 1939. It could also be argued that the 2% tax is not a direct tax on undistributed profits. It

is essentially a franchise tax measured by 2% of undistributed profits.

The Term Resident Under the Income Tax Law

A resident of New York is taxed on his entire net income derived from all sources during the taxable year. The regulations define a resident as a person domiciled in New York who has a permanent place of abode in the State. A resident may also be a person domiciled in New York, with a permanent place of abode outside the State, who spends in the aggregate more than 30 days of the taxable year in the State. Also taxed as a resident is a person domiciled outside New York who maintains a permanent place of abode within the State and who spends in the aggregate more than 183 days of the year in the State.

One of our members would like to know the extent to which a person is taxable under the following circumstances. For 11 months during the year A is domiciled in New York and has a permanent place of abode in the State. On December 1 he establishes a domicile and a permanent place of abode in Liberia. On December 1 of the following year A again changes his domicile to New York and again sets up a permanent place of abode in New York.

If the change of domicile to Liberia is bona fide then A is taxable as a resident for 11 months and as a non-resident for 1 month. If the change of domicile back to New York is bona fide then in that year, A is taxable as a non-resident for 11 months and as a resident for 1 month.

If it is held that there has been no change in domicile, but merely a change in permanent place of abode, then the Liberian residence would in no way affect A's status as a resident for the full year. He is domiciled in New York and, regardless of his permanent place of abode, has spent more than 30 days of the taxable year within the State.

In the following year when A again sets up an abode in New York he will be subject to tax as a resident on his entire income for the year if he is present in New York for more than 30 days. That would be the case if he is present continuously from December 1 to December 31. If A is present in the State from December 2 to December 31 he would be taxable only on income earned during that period.

Accounting at the SEC

Conducted by Louis H. Rappaport, C.P.A.

Listing Applications—Accountant's Approval of Accounting Proposed to be Followed

The following note is not concerned directly with accounting at the SEC; it relates, however, to the requirements of the New York Stock Exchange and is, therefore, indirectly related to the SEC.

A company whose common stock is listed for trading on the New York Stock Exchange recently filed an application to list an additional block of its common stock. The additional stock was to be issued in connection with the acquisition of another company which was engaged in the same type of business as the listed company. In the narrative section of the listing application, the company disclosed the purpose of the issue and recited the accounting which it would observe in connection with the issuance of stock to which the listing application related. The listed company said, in effect, that it would record the stock at its fair value which was considered to be the quoted market price on the date it entered into the agreement to acquire the other company. The listed company also stated that on its books it would record the assets of the acquired company at the same amounts at which they appeared on the books of the latter company. The excess of consideration paid (measured by the market value of the stock to be issued) over the book amount of net assets acquired, said the company, would be charged to goodwill. The company stated further that it had no plans for writing off such goodwill.

The company sent a copy of the application to its accountants saying that the Exchange had requested the accountants to sign that portion of the application which recited the accounting to be followed in respect of the acquisition. The accountants were puzzled by the Exchange's request and wondered what purpose would be served by signing the application as requested. The accountants agreed with the proposed accounting to be followed by the company but were at a loss to understand how such approval would be conveyed merely by signing the application alongside the text dealing with the accounting policy.

The accountants called the Department of Stock List of the New York Stock Exchange with a view to ascertaining the reason for the Exchange's request. The Department informed the accountants that in the past some listed companies had recited the accounting proposed to be followed in connection

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with acquisitions, mergers and other transactions without consulting their certifying accountants. Subsequently, during the annual audit, the certifying accountants might take exception to the accounting followed by their client in respect of the stock issued in connection with the particular transaction. Although the accountants might not agree, the client might point to the fact that the accounting had been recited in a listing application and presumably the Exchange approved it. In order that the certifying accountants might be informed in advance regarding the accounting proposed to be followed in connection with material transactions of this type, the Exchange now requires the company's independent accountants to express their approval or disapproval of the accounting for the transaction at the time of filing the listing application. This approval, said the Exchange, can be accomplished either by having the certifying accountant sign alongside the material in the listing application, or by writing a letter to the Exchange expressing such approval.

A mere signature on a copy of the listing application may indicate that the signer has seen the application, but it does not necessarily indicate his approval or disapproval of the matter in question. When an accountant puts his signature on a document, there ought to be no doubt as to its significance. It seems to this writer that the accountants should state their views in a letter or in a similar manner which clearly sets forth their opinion.

Office and Staff Management

A forum for the exchange of views and information on all aspects of the administration of an accounting practice.

Conducted by MAX BLOCK, C.P.A.

"The Charge of the Light Brigade" and Its Moral to Accountants . . . Register of Letters Received and Sent Out . . . Will Your Bank Soon Require a "Marketing Audit"? . . . Controlling "Out of Town" Tax Compliance.

"The Charge of the Light Brigade" and Its Moral to Accountants

There is no tale more tragic than that told in Tennyson's poetry classic about the brigade that was ordered to certain doom. The reason, history relates, was faulty communication.

On several occasions faulty communication has been singled out in this column as a problem confronting accountants, which deserved much of their time and attention. Recently, the writer had the opportunity to examine a manual for manual writers that contained a very detailed set of rules and suggestions on how to achieve in communications a very high degree of accuracy, lucidity, and effectiveness as to compliance.

MAX BLOCK, C.P.A. *(N. Y., Pa.) is a former chairman of the Committee on Administration of Accountant's Practice of the New York State Society of Certified Public Accountants. He is a lecturer at The City College of New York in the graduate course on Accounting Practice. Mr. Block is a member of the firm of Anchin, Block & Anchin.*

The manual, entitled *How to Communicate Policy and Procedure,* was prepared by Joseph D. Cooper, an experienced policy and procedures analyst, and is published by the Bureau of Business Practice, National Foremen's Institute.

In the preface the author describes the book's objective, very modestly, as follows: "This book deals with an important management technique: how to communicate policies and procedures within business organizations. It deals with an increasingly common problem of mass and multiplicity of instructions by telling how to coordinate them within loose-leaf systems."

The book is an outstanding demonstration of the importance of the problem of communication and of its many facets. It contains so much material that it appears to exhaust the subject, but none of it is superfluous. It is a very worthy guide for the organization of communication procedures and should be beneficial to those who have need of it. It clearly is intended for persons who devote all, or a substantial

portion, of their time to the subject of drafting manuals of policy and instructions within business organizations. For that reason it may not have widespread appeal amongst accountants. However, those practitioners who issue staff manuals, and have well developed staff bulletin procedures will find some worthwhile "nuggets" in it. Accountants who concern themselves with management guidance of clients may have occasion to recommend to them the observance of the many principles expounded by the author.

Register of Letters Received and Sent Out

The receipt and mailing of important letters and instruments may, at some time, be subject to proof. Particularly, the mailing of tax returns, requests for extensions, refund claims, and other documents of equal importance, warrant the maximum care. Letters embodying contractual terms and other significant material are other instances where proof of mailing, or of receipt, may be of great importance.

Despite the use of registered and certified mail, some accounting and law offices, and government agencies use registers for incoming and outgoing mail of importance. A wide, bound book is commonly used, with separate pages for mail in and out, and a new page is started each day. As to each communication a record is made of the name of the entity from whom received, or to whom sent; a brief reference to the subject covered; and a listing of the attachments, if any.

Will Your Bank Soon Require a "Marketing Audit"?

The above title is taken from a monthly bulletin of an important market research organization. An insight into the major theme of the bulletin is furnished by the following excerpt:

> Any company that limits its role to merely making its products available to the public is traveling an increasingly rocky road, no matter how successfully it may have performed this function in the past. The health of a company today must be judged by its ability to capture an increasing share of the *potential* market for its products in the battle for the consumer's dollar. It is therefor logical to expect that, as time goes on, bankers and businessmen in general will want—and even demand—"marketing audits" of the firms with which they deal.

It is quite apparent that our business enterprises are moving so rapidly into new and higher ground that credit grantors, of necessity, may have to develop additional criteria for appraising credit risks, particularly where large amounts are involved or where funds are made available on a rotating or virtually continuous basis.

Accountants who are management conscious will find the bulletin provocative. Copies may be obtained from Henry Bach Associates, Inc., New York City.

Controlling "Out of Town" Tax Compliance

As clients extend their activities into other states, cities, counties, etc., (foreign countries are not being overlooked), responsibilities for compliance with the tax laws of those communities are incurred. Where clients depend on their accountants to keep them posted on such matters, the accountants are confronted with a control problem—namely, how to sift the flow of tax material from all parts of the country and relate it to specific clients. Here are some thoughts on this problem:

1. State tax services are available, as the primary sources of tax information.
2. A geographic card file will facilitate the relation of tax material to clients.

The card file functions as follows: A card is prepared with the caption, to illustrate, "Miami, Dade County, Flor-

(Continued on page 741)

Payroll Tax Notes

Conducted by Samuel S. Ress

Subsidiary Unemployment Insurance Contributions . . . Late Reporting of Employment Data . . . Newly-Covered Self-Employed . . . Effective January 1, 1957—Increase in Social Security Tax Rates . . . Farm Workers 1957 Social Security Tax Status . . . Federal Unemployment Tax for 1956 Payable in Full by January 31, 1957 . . . Election to Withhold on Sick Pay in 1957.

Subsidiary Unemployment Insurance Contributions

When the unemployment insurance law was amended in 1951 so as to provide for *experience rating* in unemployment insurance, one of the provisions in the Hughes-Brees Act called for the imposition of the subsidiary unemployment insurance contribution under certain conditions. Because the *general account,* to which employers' negative balances are charged, showed a balance at June 30, 1956 amounting to less than one and one-half per cent of all the taxable payrolls of all employers in the calendar year 1955, the subsidiary contribution provisions of the law went into effect.

Samuel S. Ress, *an Associate Member of our Society since 1936, is a member of the New York and Massachusetts Bar. He is engaged in public practice in his own office in New York City specializing in payroll taxation and labor-management matters.*

Dr. Ress is a member of the Society's Committee on New York State Taxation and Chairman of its Subcommittee on Unemployment Insurance.

Consequently, on January 1, 1957, employers in New York State, with the exception of certain newly-covered employers, will be required to pay an additional unemployment insurance tax of .3 per cent of their taxable payroll, regardless of how good or poor their unemployment insurance *experience* may have been. Employees with poor *experience* will thus have to pay 3 per cent of their taxable payroll to New York State, although the maximum credit of 2.7 per cent for federal unemployment tax remains unchanged. The combined State and Federal taxes under these circumstances therefore amounts to 3.3 per cent instead of the maximum of 3 per cent which was contemplated when the federal unemployment tax law was enacted.

Employers with the best *experience* record will be required to pay to New York State .8 per cent of their taxable payroll instead of .5 per cent which would normally have been applied for the year 1957.

Late Reporting of Employment Data

In order to settle a claim for benefits promptly and accurately, the Division of Employment asks the employer

whether the benefit claimant is unemployed, the period of employment and the earnings in the preceding 52 weeks. Each employer is required to furnish the information on a form L.O.12.11 if it is the claimant's last employer, or on a form LO 12 if the employer was named by the claimant as one of his employers during the previous 52 weeks. If the employer fails to complete and return a *Request for Employment and Wage Data* (Form LO 12.11 or LO 12) within 7 days after it was mailed to him, a mandatory penalty of $10 is assessed against the employer with respect to each such failure to file on time, unless the employer can satisfy the Division of Employment that the failure was due to circumstances beyond his control. Reasons for late reply which have been held to be insufficient to constitute circumstances beyond the employer's control include:

Employer on vacation—

Accumulation of mail left for accountant to handle—

Change of address without notice to the Division—

Transmittal delay by post office; it was held that the postmark date stamped on the letter is conclusive—

Response to a previous request relating to a different base period—

Difficulty of tracing employment records of chain store employees—

Negligence of employees—

Absence of employer—

Vacation shutdown—

Payroll records left with purchaser of business who continued operations.

It would appear to be clearly appropriate for the Commissioner to reevaluate these circumstances since most of them appear to constitute valid ground for waiving the imposition of the penalty.

Newly-Covered Self-Employed

A new brochure relating to newly-covered professions has been made available by the Social Security Administration of the United States Department of Health, Education and Welfare. This booklet explains the provisions of the 1956 amendments to the Social Security Law applicable to lawyers, veterinarians, dentists, and others.

Effective January 1, 1957—Increase in Social Security Tax Rates

The rate of tax on both employer and employee will increase to 2¼% for taxable wages paid on and after January 1, 1957, regardless of period for which the wages had been earned. If back pay is owing, or if an employee had already reached his $4200.00 taxable wage ceiling in 1956, a saving of tax (employer-employee) amounting to 4½ per cent of the otherwise taxable payroll can result by making the wage payment prior to January 1, 1957.

Farm Workers 1957 Social Security Tax Status

On and after January 1, 1957, an employer of agricultural labor is subject to the social security tax (on cash portion of wages) if the employee:

(1) receives cash wages of at least $150.00 during the calendar year; or,

(2) is employed on 20 or more days, with cash wages payable on a time basis regardless of the quantity of work produced or harvested.

Federal Unemployment Tax for 1956 Payable in Full by January 31, 1957

The quarterly installment method of paying the federal unemployment tax payable by the employer had been in effect only for taxable years preceding 1955. Those employers who require more time to pay the Federal Unemployment Tax will have to pay interest at the rate of 6% per annum on any balances owing on 1956 taxable payroll and not remitted by January 31, 1957. However, applications for extension of

time for filing the federal unemployment tax return should be filed under certain circumstances to safeguard against the imposition of an additional federal unemployment tax where 1956 state contributions have not been fully paid prior to February 1, 1957, or where the amount of the employer's experience rate tax credit is in dispute or has not been finally determined by the aforesaid date. The additional federal unemployment tax assessed is generally the amount unpaid to the state unemployment insurance fund plus 10% of the 1956 state unemployment insurance tax paid after January 31, 1957.

Election to Withhold on Sick Pay in 1957

An employer who directly makes "loss of wage" payments for sickness or injury to his employee in 1957, may elect to refrain from deducting income tax from the tax-exempt portion of such payments. Amounts received by an employee under an employer-financed accident and health plan are not taxable income to the employee up to a weekly rate of $100 a week, except that payments for loss of wages for the first seven calendar days of a period of absence due to sickness are taxable unless the employee is hospitalized for at least one day during the period of absence.

In any event, employers are required to have sufficient information of amount and weekly rate of each payment and to keep a record of beginning and ending dates of each employee's absence from work due to sickness or personal injury. If the employer elects to withhold income tax from "sick pay" under a "wage continuation" plan, the employee will, of course, take the proper withholding tax credit on his individual income tax return.

If the employer elects not to withhold, he should be advised to observe the following:

(1) The amount of each payment and the tax-exempt amount should be separately stated.

(2) A written statement should be obtained, signed by the employee, specifying whether the absence from work was due to a personal injury or sickness. If absence was due to sickness, the employee should also state whether he was hospitalized for at least one day during the absence period.

If the "sick pay" benefit is paid by an insurance company, a trust, a state agency, or another party, the income tax should not be withheld from the sick person's benefit by the paying agency.

Office and Staff Management

(Continued from page 738)

ida." On that card are listed the names of clients who, because of some described activity in that city, are subject to city, county, or state taxation. Whenever a tax service reports matters affecting taxpayers doing business in Florida, or in Miami, or in Dade County, one need only remove the appropriate card from the file to find out what clients might be affected.

Official Decisions and Releases

Opinion in the Appeal of *Agran* v *Shapiro* . . .
Voted Resolutions—Board of Regents . . . Renewal of Treasury Cards

Opinion in the Appeal of *Agran* v *Shapiro*—the Appellate Department of the Superior Court, Los Angeles County

A reading of the record satisfies us that the trial court proceeded in accordance with the views expressed in our previous opinion (*Agran* v. *Shapiro* (1954), 127 Cal. App. 2d Supp. 807) which constitutes the law of the case, and we see no reason to depart from what is said therein. The findings are supported by the evidence.

Neither are we impressed with the plaintiff's argument that the trial court erred in not making a finding to the effect that the Treasury Department treats alike enrolled agents and enrolled attorneys and that such a finding, if made, would have required the conclusion that this constitutes a practical construction by the Department of the regulation in question that an enrolled agent in connection with matters arising under the Internal Revenue Code is authorized to do and perform acts which otherwise constitute the practice of law.

Reduced to its simplest form, plaintiff's argument in effect is this: by virtue of the Treasury Regulation (C.F.R. 10.2) an enrolled agent though a nonlawyer is at liberty to perform any and all services and give advice upon legal questions which constitute the practice of law within the meaning of that term as generally understood so long as the work is performed or the advice is given in connection with a matter involving or arising under the federal Internal Revenue Code and pending before the Treasury Department. This is pointed up by plaintiff's suggestion that the decision in the *Bercu* case (78 N.Y.S. 2d 209) would have been different if the respondent there had been enrolled (which he was not) as an agent by the Treasury Department, but if that court was correct, as we believe it was, in concluding that the services rendered by Mr. Bercu constituted the practice of law, the necessary effect of plaintiff's argument is that a state may not regulate the practice of law within its borders by prohibiting laymen from practicing law at least insofar as related to matters and questions arising under the Internal Revenue Code so that what constitutes the practice of law no longer depends upon what is done but by whom. If this be true, the same act which would constitute the practice of law under the law of this state if performed here and which if performed by a nonlawyer not enrolled as an agent by the Treasury Department would subject him to criminal prosecution, would not constitute the practice of law if performed by a nonlawyer so enrolled. To accept the plaintiff's argument would simply mean that the individual states are in effect deprived of their traditional and long-recognized right to

regulate the practice of law within their borders at least insofar as such practice involves matters of so-called "tax law." If this is to be the rule we feel it should be announced by some higher authority.

Nothing said herein or in our previous opinion implies a holding, as plaintiff seems to think, that the Treasury Department may not prescribe the qualifications of those whom it will recognize as agents or attorneys of others having business with the Department but rather that by such recognition it may not confer upon persons who are not members of the bar authority to perform services within a state which, under its laws, constitute the practice of law in violation of that state's laws.

The judgment is affirmed.

Dated Sept. 20, 1956.

PATROSSO,
Judge.

I concur: Kauffman, Judge.

I concur in the judgment: Edward T. Bishop, Presiding Judge.

Voted Resolutions—Board of Regents
The University of the State of New York

Adopted September 28, 1956

Upon the report of the Regents Committee on Discipline, made in accordance with the provisions of chapter 514 of the Laws of 1945, it was

Voted. That the determination of the Certified Public Accountancy Committee on Grievances in the matter of the application for the revocation of the certified public accountant certificate heretofore granted to Jesse B. Cogen, Mt. Vernon, be accepted and sustained; that, in compliance with the recommendation of said committee, certificate No. 11116, issued under date of February 1, 1946, to said Jesse B. Cogen, permitting him to practice as a certified public accountant in the State of New York, and his registration or registrations as a certified public accountant, wherever they may appear, be suspended for a period of three months from the date of service of the order effecting such suspension; and that the Commissioner of Education be empowered and directed to execute, for and on behalf of the Board of Regents, all orders necessary to accept the determination of said Committee on Grievances and to carry out the terms of this vote.

Adopted September 28, 1956

Upon the report of the Regents Committee on Discipline, made in accordance with the provisions of chapter 514 of the Laws of 1945, it was

Voted. That the findings of the Certified Public Accountancy Committee on Grievances in the matter of the application for the revocation of the certified public accountant certificate (No. 11026 dated May 18, 1945) heretofore granted to Leon Rubin, North Miami, Florida, be accepted and sustained; but that the recommendation of said Committee on Grievances that the certified public accountant certificate heretofore issued to said Leon Rubin be suspended for a period of one year, be modified, and that said Leon Rubin be censured and reprimanded; that, because of his physical condition, Leon Rubin be not required to appear before the Board of Regents to receive said censure and reprimand, but that said censure and reprimand be sent to him by mail.

Renewal of Treasury Enrollment Cards

The Treasury Department anticipates that 62,000 of its enrollment cards will expire and be subject to renewal in 1957. To provide means for the processing of such peak load a renewal procedure was prescribed in an amendment of Section 10.6(d) of Department Circular 230 published in the Federal Register on October 17, 1956.

It is anticipated that renewal forms will be available early in December at the office of the District Director of Internal Revenue Service of the district within which an applicant conducts his practice except that if such place of practice is in the Brooklyn, or Upper Manhattan or Lower Manhattan district such form will be available at the office of the Regional Commissioner, New York, New York.

Renewal Procedure

Forms: An application for the renewal of an enrollment card may be made by filing *Form 23A* in duplicate with the enrollment card last issued attached thereto.

Place of filing: Form 23A must be filed as aforesaid in the office of the District Director of Internal Revenue of the district in which an applicant conducts his practice, *unless* such place of practice is either in the Brooklyn or Upper Manhattan or Lower Manhattan District, in which case the applicant must file at the office of the Regional Commissioner of Internal Revenue, New York, New York.

Processing of renewal applications: New enrollment cards will be issued by the Intelligence Division within each of the above-designated offices where there is a fulfillment of the following conditions:

(a) If the renewal form is fully made out and properly executed.

(b) If the answers to the questions set forth in said form are favorable to the applicant and there is no reason to challenge the truth thereof or other basis to raise a question as to whether the applicant measures up to the standards prescribed in the regulations set forth in Department Circular 230.

(c) If the renewal application is filed either within one year before, or one year after the expiration of the card last issued.

Failure to attach the enrollment card last issued to renewal application: Where the applicant is unable to attach his card last issued, a detailed explanation of the reason for such inability should be attached to his renewal application.

Provision against disruption of enrollments: Where the renewal application fulfills the conditions above specified, a new card will be promptly issued. Questionable applications will be forwarded to the Director of Practice for processing pending which, temporary cards may be issued by him depending on the circumstances of the case.

Original applications: As heretofore, original applications must be filed at the office of the Director of Practice, Internal Revenue Building, Washington, D. C.

George C. Lea
Director of Practice

Ed. Note: As a service to its members, the Society will enclose two copies of *Form 23A* with the mailing of the January 1957 issue of the *NYCPA*. This will obviate the necessity for our members to request the forms from the Internal Revenue Service.

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*Reviewed by the Editor.

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